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Secretary of State

By:

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Assistant Secretary of State

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PUERTO RICO TOURISM COMPANY

REGULATION PROMULGATED TO GOVERN THE CONDITIONS FOR GRANTING TAX EXEMPTIONS AND OTHER TAX INCENTIVES PURSUANT TO THE PROVISIONS OF ARTICLE 9(B) OF THE PUERTO RICO TOURISM DEVELOPMENT ACT OF 1993, AS AMENDED, ACT NO. 78 OF SEPTEMBER 10, 1993, AS AMENDED.

§1-1. Authority. This Regulation is promulgated by virtue of Act No. 10 of June 18, 1970, as amended, and pursuant to the provisions of Act No. 170 of August 12, 1988, as amended, and of the Puerto Rico Tourism Development Act of 1993, Act No. 78 of September 10, 1993, as amended.

§1-2. "Act"; Defined Term. Any reference to the "Act" herein shall be deemed to be to the Puerto Rico Tourism Development Act of 1993, Act No. 78 of September 10, 1993.

§1-3. Defined Terms. Any term not defined herein shall have the meaning given it in the Act.

§2(d)-1. Condohotels. Condohotel means the cluster of structures, building units, villas or group of buildings converted to the horizontal property regime, and which comply with the requirements of a Hotel; in which not less than fifteen (15) of the rooms, apartments or villas are dedicated to lodgings for travellers at all times through an integrated rental program. The individual buildings which comprise the

group of buildings, or cluster of structures need not have been submitted to the same horizontal property regime, as long as they are operated under the same integrated rental program and they comply independently with the requirements of a Hotel as defined in the following paragraph. There may be more than one integrated rental program in a structure, building, villa or cluster thereof which is a Condohotel, in which case the owner of a unit may change his program as long as he arranges for an amendment to his individual Tax Exemption Concession to reflect the change of his unit to the master Concession of another integrated rental program, and which change is reflected in said master Concession according to the provisions of Section 9(c)-1(a) of this Regulation.

The phrase "which complies with the requirements of a Hotel" means that it has all of the physical facilities, or access thereto, it provides Hotel service and complies with the Innkeepers Act. Furthermore, it must comply with the Regulation for Minimum Requirements of Hostelries and Inns of Puerto Rico promulgated by the Tourism Company or any other similar successor regulation. The owners of the individual units which are part of the integrated rental program may have use of an area to which only they have access ("owner's closet") to keep their personal belongings.

§2(d)-2. Number of Rooms or Apartments in a Condohotel. The minimum number of rooms, apartments, or villas necessary for a Condohotel to be considered an Eligible Business is fifteen

(15). For purposes of compliance herewith, there shall be considered those units which have a bathroom and private entrance.

§2(d)-3. Time Share. Time Share means the right to use a unit in a building, structure or villa for a limited period of time each year. A contribution in cash or in any other manner made for the purchase of a time share shall not be considered an Eligible Investment under the Act.

§2(d)-4. Examples. (i) A villa in a development which complies with all of the requirements of Condohotel, has three (3) rooms each with a bathroom and each with a private entrance. If the owner of the villa dedicates it to the integrated rental program, the villa shall be deemed to be contributing three (3) rooms to the requisite fifteen (15).

(ii) An apartment in a development which complies with all of the requirements of a Condohotel, has three (3) rooms each with private bathroom, but the apartment only has one entrance for all of the rooms. For purposes of compliance with the requisite fifteen (15) units, the apartment will count as one unit.

§2(d)-5. Integrated Rental Program. The phrase "through an integrated rental program" means that there is a Person who operates a business which is dedicated to renting the units of the building or group of buildings, structure or villas which are dedicated to lodging for travellers. This requirement shall not be satisfied where in a building or group of

buildings, structures or villas, the owners of the units individually dedicate them to lodgings for travellers. Such phrase includes any rental program, regardless of the manner in which the owners of the units decide to distribute the profits produced by the rental thereof. In those cases where the operator of the integrated rental program ceases to operate such program, which must be notified to the Director within fifteen (15) days of such cessation by the operator, the owners of the individual units which are part of the program shall enjoy a grace period of three (3) months, counted as of the date of termination of the program, to arrange for another integrated rental program under the same Concession, whether it be a newly created program or a program existing on the same premises, without losing the benefits of the Concession. Any income derived from the rental of the unit during the time transpired between the date of termination of the integrated rental program to which the unit was incorporated and the date of entry into the new program, as long as it occurs within said three (3) month term, shall be considered Tourism Development Income. In order for said income to be considered Tourism Development Income, however, the owner of the unit must have paid the occupancy tax required by law and the unit must have been rented for tourism purposes. Should the three (3) month period transpire without the unit having been incorporated into a new integrated rental program, the Tax Exemption Concession for said unit shall be

deemed to be terminated retroactively to the date of termination of the old integrated rental program. Said three (3) month period may be extended through prior authorization of the Director when he believes that it is in the best interests of Puerto Rican tourism.

§2(e)-1. Guest House.

Guest House means any building, part thereof, or group of buildings approved by the Puerto Rico Tourism Company to be operated for tourism purposes. It must consist of not less than seven (7) rooms for travellers, provide administrative personnel twenty-four (24) hours a day, and provide applicable hotel services according to the Innkeepers Act and the Regulation for Minimum Requirements of Hostelries and Inns of Puerto Rico promulgated, implemented and administered by the Puerto Rico Tourism Company.

§2(e)-2. Small Hostelries.

Any small hostelry which complies with the requirements of a Guest House or Tourism Villa shall be considered as such for purposes of the Act. In this manner, the Tourism Villas and small Hotels which otherwise do not comply with the Act's requirements for Hotels may enjoy the benefits of the Act, as long as they comply with the requirements for a Guest House or Tourism Villa under the Act.

§2(f)-1. New Business.

New Business means a business which is not operating at the time that an application for a Concession under the Act is

duly filed and which will be engaged in a Tourism Activity using physical facilities which have not been used, or which have been used only incidentally, in a Tourism Activity during the period of thirty-six (36) months prior to the date of filing of the application. A Condohotel shall only qualify as a New Business if the units which comprise it are acquired from the entity which developed or constructed the same, and have not been used prior to said acquisition for any purpose, in which case the purchaser shall have a grace period of four (4) months from the date of the deed of purchase and sale of the unit to incorporate the same into an integrated rental program.

The Developers of a Condohotel may also dedicate the unsold units of their Condohotel to an integrated rental program on a temporary basis without impairing the possibility that any subsequent purchasers of said units acquire the benefits of the Act, including the right to receive the tourism investment tax credit provided for in Article 5 of the Act and the corresponding sections of this Regulation. The Developers of a Condohotel who wish to take advantage of this benefit shall file an application for a Concession under the Act pursuant to the provisions of the last paragraph of Section 9(c)-1(a) hereof for purposes of obtaining solely and exclusively exemption from the payment of income taxes, property taxes, municipal licenses, and other municipal excise taxes. The Condohotel Concession shall not grant any tax

credit whatsoever to the Developer for purposes of the credits provided for in Articles 5(a) and 5(e) of the Act. The Developer may not use any unit pursuant to the provisions of this paragraph for a period exceeding ten years. The benefits of the Act which will be available to the subsequent purchaser of any unit used by the Developer under the provisions hereof shall be the same that would have been available if the unit had never been used by the Developer, except for the fact that:

(i) the tourism investment tax credit to which the subsequent purchaser will be entitled shall be the lesser amount between: (a) fifty percent (50%) of the cash contributed towards the purchase of the unit, and (b) ten percent (10%) of the lesser amount between the price at which the first comparable unit in the same Condohotel was sold immediately after commencement of the integrated rental program, and the price at which the unit was purchased by the subsequent purchaser, and

(ii) the term of ten (10) years during which the subsequent purchaser shall be entitled to the benefits granted by the Act shall be reduced by the amount of time during which the Developer used the unit.

§2(f)-2. Examples. (i) The CC Guest House, a 10 room hostelry, was in operation from January, 1985 until December, 1990. From the time it closed in 1990, the building where the Guest House was located has not been used. Mr. CC wishes to

reopen the Guest House and in February, 1994, he files an application for tax exemption under the Act. The "new" CC Guest House will qualify as a New Business under Section 2(f) of the Act. The Guest House will qualify as a New Business independently of whether it had a Tax Exemption Grant under the Tourism Incentives Act of 1983, from 1985 to 1990.

(ii) Developer ZZ developed and built "Condohotel ZZ", a complex consisting of twenty-five (25) identical villas which were dedicated to the same integrated rental program. ZZ sold twenty-three (23) of the villas for \$100,000 each and, although the villas were immediately dedicated to said program, ZZ was not able to sell the remaining two (2) villas. If ZZ wished to dedicate those last two villas to the integrated rental program on a temporary basis without impairing the possibility that the future purchaser of each villa be entitled to the tourism investment tax credit provided for in Section 2(f)-1 herein, the procedure to be followed will be: (a) ZZ will file an application for a Concession for each of the two villas requesting exemption from the payment of income, property and municipal license taxes and other municipal excise taxes only; (b) ZZ will incorporate the villas into the integrated rental program temporarily; and (c) when ZZ sells each of the two villas, the purchaser of each villa shall file an application for a Concession pursuant to the provisions of the last paragraph of Section 9(c)-1(a) of this Regulation just as if he were

obtaining a unit which had not been used prior to the date of its acquisition.

The tourism investment tax credit to which each purchaser will be entitled will be the lesser amount between fifty (50%) of the cash contributed towards the purchase of the unit and \$10,000. In order to determine the tax exemption period for the new purchasers, the period of time during which ZZ used the units on a temporary basis pursuant to the provisions of Section 2(f)-1 shall be deducted from the ten-year period to which grantees under the Act are entitled.

\$2(g)-1. Existing Business. Existing Business means a business which is dedicated to a Tourism Activity at the time an application for a Concession under the Act is duly filed, or which otherwise does not qualify as a New Business under the Act, and which engages in a substantial renovation or expansion of the existing physical facilities to be used in a Tourism Activity.

\$2(g)-2. Substantial Renovation or Expansion.

(a) A substantial renovation or expansion of the existing physical facilities entails an investment directed towards renovating, remodeling, or expanding the existing physical facilities, as long as the substantial renovation or expansion: (i) has an economic life of at least five (5) years and (ii) it is in real property, be it by nature or by destination. The Director shall determine the dollar amount required of each substantial renovation or expansion on a case

by case basis. In the specific case of hostelries of twenty-five (25) rooms or less, and of hostelries under the Puerto Rican Parador program sponsored by the Puerto Rico Tourism Company (independently of their size) which file an application to obtain a Tax Exemption Concession within three (3) years of the date of effectiveness of this Regulation, the Director shall take into consideration the amount of money invested during the three (3) years prior to the date of the filing of the application to determine whether the Petitioner's proposed investment project qualifies as a substantial renovation or expansion. The funds invested during the three (3) years prior to the date of the filing of the application, however, shall not be taken into consideration to compute the tourism investment tax credit to which the Exempt Business shall be entitled.

(b) In the specific case of businesses which apply for a Concession which only includes exemption from the payment of property, excise and municipal license taxes only, that is, which excludes exemption from the payment of income taxes, the term "substantial renovation or expansion" shall not include what is specified in items (i) and (ii) of the first sentence of this Section 2(g)-2. In these cases, the Director shall determine the type of investment which the business must make in order to offer a product in optimum operating conditions, and that investment shall be the one to be considered as a

substantial renovation or expansion for purposes of this section.

§2(g)-3. Examples. (i) Among the projects which are included in the definition of substantial renovation for purposes of Section 2(g)-2(a), as long as they comply with the minimum cost requirements which shall be determined by the Director on a case by case basis, are: A new wing or annex to a building, the reconstruction or remodeling of a kitchen or activities hall, or the installation of a new elevator system. On the other hand, an investment made for purchasing bed linen, television sets, or any other personal property shall not be considered to be a substantial renovation under Section 2(g)-2(a), but it could be considered to be a substantial renovation for cases under Section 2(g)-2(b).

(ii) Parador X, Inc., a fifteen (15)-room hostelry which is in an unstable financial condition, requests a Tax Exemption Concession under the Act. Since it is not able to obtain the financing necessary to make a substantial renovation or expansion for purposes of Section 2(g)-2(a) hereof, X requests that it be granted exemption from the payment of property, excise and municipal license taxes only. The Director determines that due to the good physical condition of the Parador, maintaining X in optimum operating conditions only requires an investment directed to purchasing new television sets, curtains, and bed linen for each of its rooms. The Director may approve a Concession for Parador X

which excludes exemption from the payment of income taxes, such exemption being contingent on X complying with the aforementioned conditions regarding the investment in personal property for its facilities.

§2(h)-1. Tourism Activity. Tourism Activity means:

(1) the ownership and/or administration of: Hotels, Condohotels, Puerto Rican Paradors, and Guest Houses (excluding the operation of casinos, game rooms and similar activities), theme parks, golf courses operated by or associated with a Hotel which is an Exempt Business, marinas for tourism purposes, facilities around port areas and other facilities which, due to the special attraction derived from their use as a source of active or passive entertainment, are a stimulus to internal or external tourism, as long as the Director determines that such operation is necessary and convenient for the development of tourism in Puerto Rico;

(2) the operation of a business dedicated to renting to an Exempt Business property dedicated to an activity covered by subparagraph (1) hereof, except that nothing provided herein shall apply to agreements called finance lease agreements;

(3) the development and/or administration of natural resources to be used as a source of active or passive entertainment, including, but not limited to, caves, forests, natural reserves, lakes and canyons, as long as the Director determines that such development and/or administration is

necessary and convenient for the development of tourism in Puerto Rico.

§2(h)-2. Ownership and/or Administration. It is not necessary that the ownership and/or the administration referred to in subparagraph (1) above reside within the same Person. Both activities qualify separately as a Tourism Activity regardless of whether they are undertaken by the same Person.

§2(h)-3. Golf Courses. Golf courses must be associated with or operated by a Hotel which is an Exempt Business in order to be considered as a Tourism Activity. The phrase "associated with a Hotel" means that there is a formal agreement between the golf course and the Hotel which is an Exempt Business whereby the Hotel's guests enjoy the right to use the golf course. Golf courses which are not operated by a Hotel, but are merely associated with a Hotel which is an Exempt Business, shall maintain specific records regarding the income generated by the golfers who come from the Hotel with which the course is associated. Only said income shall be considered Tourism Development Income for purposes of income tax exemption under Article 3(a)(1) of the Act and for purposes of municipal license tax exemption under Article 3(a)(3) thereof. The percentage of exemption from the payment of property taxes shall be the percentage of income generated by the golf course which is Tourism Development Income multiplied by the exemption rate from the payment of property taxes provided for by the Tax Exemption Concession.

§2(h)-4. Renting Property Dedicated to a Tourism Activity.

In order to be considered a Tourism Activity, the business which is dedicated to renting property dedicated to a Tourism Activity may not fall within the guidelines published by the Secretary in the Administrative Rulings which regulate the finance lease business. A business which is dedicated to finance leases, as set forth in said Administrative Rulings, is not considered to be dedicated to a Tourism Activity.

§2(h)-5. Theme Parks. The term "Theme park" includes any facility of a certain magnitude and with permanent structure(s) which under a specific or unifying theme provides for the recreation, leisure and enjoyment of residents and visitors. Its facilities shall be developed around a natural, historical and/or cultural resource, a scientific research subject, or a special environment, created by artificial means, which shall constitute an attraction to foreign or local tourists due to its peculiar characteristics, the singularity of the theme chosen and/or the theme's relationship with Puerto Rican culture and idiosyncrasy. For example, some themes considered within this term would be:

1. Aquatic theme - as a general rule it shall be located with direct access to the ocean, bays, lakes, lagoons, rivers or, in the alternative, the theme shall be designed and developed based on the element of water.

2. Cultural or historical theme - it shall use elements of our cultural history. Examples: theaters with plays, artisan village and IMAX theaters (with special movies on the Caribbean).
3. Natural resources theme - it shall contain attractions related to our natural resources or representative activities (forests, flora and fauna).

§2(h)-6. Tourist Marinas. Tourist Marina means a project at the edge of the water with facilities that are to be dedicated principally to the use of local or international tourism deriving the majority of its income therefrom. Its facilities and equipment shall comply with the requirements set forth by the United States Coast Guard, the Department of Natural Resources, the Public Service Commission, the Puerto Rico Ports Authority and any other regulations applicable to the operation of marinas and boats and shall include facilities for docking, fueling, the sale of food and equipment to the users. It shall also have sail or motor boats, with or without a crew, for rental to local or foreign tourists for sailing, sports fishing or other water sports, and it shall promote such services as well as services relating to the docking of visiting vessels in publications specializing in fishing, water sports, or tourism in general. The income generated by the services provided to persons who maintain their vessels at the marina permanently for their private use shall not be considered to be Tourism Development Income.

Only Tourism Development Income shall be considered for purposes of income tax exemption under Article 3(a)(1) of the Act and for purposes of the exemption from the payment of municipal license taxes under Article 3(a)(3) thereof. The percentage of exemption from the payment of property taxes shall be the percentage of income generated by the tourist marina which is Tourism Development Income multiplied by the tax exemption rate on the payment of property taxes provided by the Tax Exemption Concession.

§2(j)-1. Eligible Business. Eligible Business means any New or Existing Business dedicated to a Tourism Activity which is not covered by a tax exemption grant or resolution granted under the Industrial Incentives Act or the Tourism Incentives Act of 1983 or, if covered, such tax exemption grant or resolution is waived in favor of a Concession under the Act.

§2(j)-2. Construction Business; Operation of an Integrated Rental Program; Time Shares. The construction or development of a building or group of structures or villas which after their sale are to be used as a Condohotel shall not be considered an Eligible Business, since said business involves the construction and sale of buildings and not a Tourism Activity. The operation of an integrated rental program of units in a Condohotel is an Eligible Business, as is being the owner in fee simple of one of the individual units of a Condohotel. In the case of Time Shares, ownership of a time share shall not qualify as an Eligible Business, since the

owner of a time share is a consumer and not an Investor in the tourism industry. The operator of a time share program, however, shall be considered to be operating an Eligible Business under the Act.

§2(1)-1. Tourism Development Income. Tourism Development Income means the income of an Exempt Business resulting from the operation of a Tourism Activity, and the income resulting from the reinvestment in Puerto Rico of income of an Exempt Business obtained from a Tourism Activity, as long as such reinvestment is in a Tourism Activity.

The term "income resulting from the reinvestment in Puerto Rico of income of an Exempt Business" includes the interest generated by funds deposited in depository financial institutions in Puerto Rico, which have been reserved in the books of the Exempt Business for the improvements and/or expansions of a Tourism Activity, according to the generally accepted accounting principles (GAAP). The funds deposited for said improvements and/or expansions shall be used, in their entirety, within three (3) years of having been deposited in the aforementioned financial institutions. If they are not used within said period, the grantee shall amend its income tax returns and shall pay taxes on the interest derived for that part of the funds deposited which was not used for improvements and/or expansions within the three (3) year period. Likewise, the term "income resulting from the reinvestment in Puerto Rico of income of an Exempt Business"

shall also include the interest generated by funds deposited in depository financial institutions in Puerto Rico originating from accounts which the Exempt Business is required to maintain by the financial institution(s) which provided the financing for the Tourism Project as a condition for providing said financing. The proportion of such interest which shall be considered to be "income resulting from the reinvestment in Puerto Rico of income of an Exempt Business" shall be that proportion of the interest attributable to the Tourism Activity and not to other activities of the Exempt Business such as, for example, a casino. The Department of the Treasury of the Commonwealth of Puerto Rico shall determine the procedure to be followed to report the origin of the exempt interest.

If the Exempt Business is a Hotel, Condohotel, Parador or Guest House, the income subject to exemption shall include income from: (1) room rent and charges for services related to the Tourism Activity, (2) the sale of food and beverages, (3) the operation of retail stores within the physical facilities of the Exempt Business, but only if such retail stores are owned and operated by the Exempt Business, (4) the operation of golf courses and other sports and recreation facilities which are part of the Tourism Activity of the Exempt Business, (5) the leasing of commercial space within the Hotel, Condohotel, Parador or Guest House for the operation of businesses which provide useful services to the traveling guest.

In the specific case of the units which are part of the integrated rental program of a Condohotel, the operator of such program shall certify annually to the Department of the Treasury and to each unit owner the amount of Tourism Development Income generated by the unit. The owners of units in Condohotels shall attach a copy of said certification to their income tax returns for each year in which they report Tourism Development Income.

§2(1)-2. Examples. In general terms, any income received by the Exempt Business from a Tourism Activity shall be considered Tourism Development Income. For example, if the Exempt Business is a Hotel, Condohotel, Guest House or Puerto Rican Parador, the income derived from the rental of meeting and banquet space, concert halls, the rental of sports equipment, sports lessons, tours, the sale of food and beverages, game rooms for minors, stores operated by the Exempt Business within its physical facilities for retail sales, and the leasing of commercial space within its physical facilities for the operation of businesses which provide services to traveling guests shall be considered Tourism Development Income. On the other hand, income derived from activities which are not covered by the Tax Exemption Concession, such as, for example, the operation of a casino, shall not be considered Tourism Development Income in any case. The list above is not exhaustive but rather illustrative.

§2(1)-3. Reinvestment of Tourism Development Income. The income generated by an Exempt Business from reinvesting income derived from Tourism Development Income in a Tourism Activity in Puerto Rico, equal to or different from that of the Exempt Business, shall produce additional Tourism Development Income.

§2(m)-1. Investor. Investor shall mean anyone who makes an Eligible Investment. When the Person who makes the Eligible Investment is a Fund, the Participants shall be considered to be Investors and not the Fund.

§2(m)-2. Examples of Those Who Shall Not Be Considered Investors. The following Persons shall not be considered to be Investors: (i) those contributing money in exchange for stock or an interest in a business which constructs or develops a building or group of buildings which will be sold to Persons who will dedicate the units in the building to a Condohotel's integrated rental program, since the one who constructs or develops is in the business of constructing and selling buildings, which is not considered to be a Tourism Activity; (ii) the Developer of a Tourism Project who acquires participations in a Tourism Investment Capital Fund which will make an Eligible Investment in that same Tourism Project.

§2(n)-1. Eligible Investment. Eligible Investment means:

(1) the amount of cash which has been contributed to an Exempt Business to be used in a Tourism Activity in exchange for (i) corporate stock, if the Exempt Business is a corporation; (ii) an interest, or the increase in an interest in a

partnership or joint venture, if the Exempt Business is a partnership or joint venture; or (iii) a unit in a Condohotel, as long as the Investor is the owner of the unit and the unit is dedicated to the integrated rental program of the Condohotel for a period of ten (10) years, and is available to be used by said program for eleven (11) months of each calendar year. The operator of the Condohotel shall certify annually the number of days during which each unit was used by its owner. Failure to comply with this requirement may result in the imposition of the penalty provided in Section 8(b)(3)-1 hereof. The thirty (30) days of each year during which each Investor in a Condohotel shall have the unit at its disposal shall be determined by the operator according to the needs of the business and they need not be used consecutively.

The owners of the units of a Condohotel shall also have at their disposal up to sixty (60) days per year during which, should the volume of business of the Condohotel so permit it, they may use their units as "walk-ins." In order to benefit from this privilege, the owners of the units shall communicate with the operator of the Condohotel after eleven o'clock in the morning (11:00 a.m.) of the day on which they wish to use the unit to corroborate that the same has not been previously reserved for that day. The operator of the Condohotel shall charge a reduced daily rate, for purposes of covering the maintenance expenses, to the owners of the units who use the same under the provisions of this paragraph.

(2) the value of the lands contributed to an Exempt Business to be used in a Tourism Activity in exchange for (i) stock in the corporation, if the Exempt Business is a corporation; or (ii) an interest, or an increase in the interest, in a partnership or joint venture, if the Exempt Business is a partnership or joint venture. The value of the land contributed shall be the fair market value of the land reduced by the balance of the mortgages which encumber the land at the time of the contribution. The fair market value shall be determined based on an appraisal of such land, acceptable to the Director, performed by one or more professional appraisers duly licensed in Puerto Rico. The Director shall approve the appraisal before the land is contributed to the Exempt Business, and shall include the value of the land in the Tax Exemption Concession of the petitioner. In cases where land is contributed to the Exempt Business through surface rights lease agreements or any juridical figure of like nature for a nominal fee (for example, a yearly rent of \$1.00), which term exceeds thirty (30) years, in exchange solely and exclusively for stock in a corporation or an interest in a partnership, the Director shall reserve the right to determine whether or not such contribution shall be considered an Eligible Investment according to the circumstances of the specific case. The value of such contribution shall be the fair market value reduced by the balance of the mortgages which encumber the right contributed.

(3) contributions in cash made by a Fund to a public corporation of the Commonwealth of Puerto Rico or any of its subsidiaries, in exchange for (i) stock or an interest in an Exempt Business which said public corporations or subsidiaries own or, (ii) the subordinated debt which an Exempt Business has with said corporations or subsidiaries.

In the event that one of the contributions described in subparagraphs (1) or (2) hereof is made, such contribution shall be considered as an Eligible Investment only if it is made in the Primary Issue of the stock or partnership interests. In the event that there is a desire to make an Eligible Investment in an Exempt Business in excess of the amount provided for in the Tax Exemption Concession therefor, an amendment to the Tax Exemption Concession shall be required which reflects the additional capital contribution. The agencies, bureaus, or public corporations of the Government of Puerto Rico which make an investment to cover the expenses incurred in the design and construction of infrastructure projects for the benefit of an Exempt Business in exchange for stock or an interest in said Exempt Business shall have the option of covering said costs directly, and the amount of the contribution shall not lose its character of Eligible Investment.

In the case of Condohotels, the cash contribution shall be considered to be an Eligible Investment only if: (a) the investment is made on the basis of an appraisal of the unit

performed by an appraiser duly licensed in Puerto Rico; (b) the unit has never been used before, and (c) it is purchased from the entity that developed or constructed the same.

Any investment which funds are not used directly and in their entirety, solely and exclusively to finance (i) the expenses incurred in the acquisition of the lands, construction and habilitation of the New Business; (ii) the expenses incurred in the substantial renovation or expansion of an Existing Business; and, (iii) any contribution made by the Government of Puerto Rico for purposes of designing and constructing infrastructure projects for the benefit of the Exempt Business in exchange for stock or an interest in said Exempt Business, shall be excluded from the definition of Eligible Investment. Thus, for example, an investment which purpose is to refinance any debt related to the operation of a Tourism Activity shall not be considered to be an Eligible Investment under the Act, unless such investment qualifies under Article 2(n)(3) of the Act, which refers to cash contributions made by a Fund to a public corporation of the Commonwealth of Puerto Rico or any of its subsidiaries, in exchange for (i) stock or an interest in an Exempt Business which said corporations or subsidiaries own or, (ii) the subordinated debt which an Exempt Business has with such corporations or subsidiaries.

§2(n)-2. Examples. (A) Assume that X is an individual who contributes the amount of \$10,000 in cash to Corporation A,

which complies with the requirements of being an Exempt Business dedicated to the Tourism Activity of operating a Hotel, in exchange for 100 common shares of Corporation A issued in their Primary Issue. The contribution of X is an Eligible Investment under the terms of the Act and of this Regulation.

(B) W, X & Y, partners in a special partnership created to develop a tourism project, contribute \$25,000 each for a total partnership capital of \$75,000. Each one has a 33.3% interest in the partnership. At the end of six (6) months, W, X & Y decide that they need \$25,000 more and they convince Z to contribute this amount in exchange for a 25% interest in the partnership. Z's contribution was made in the Primary Issue of partnership interests and, therefore, is an Eligible Investment under the Act.

(C) Continuing with the same example, W, X & Y, instead of recruiting Z, decide to contribute \$8,000 each and to maintain the same percentages of participation in the partnership. That \$8,000 investment shall be considered to be made in a Primary Issue of partnership interests and, therefore, shall be an Eligible Investment under the Act.

(D) Continuing with example (B) hereof, if after some time Z decides to sell its 25% share in the partnership to ZZ, the latter would not be making an Eligible Investment under the Act since its contribution to the

partnership would not be made in the Primary Issue of partnership interests.

(E) Condohotels. Availability for eleven (11) months of each calendar year. JJ is the owner of one unit in a Condohotel and in January, 1995, he informs the operator that during 1995 he wishes to use his unit during the first week of April (7 days), the first week of July (7 days), and the last two weeks of November (14 days). The operator informs JJ that according to his schedule for 1995, his unit will be available for those dates. JJ uses his unit during the weeks mentioned. Also, JJ used his unit as a "walk-in," as set forth in Section 2(n)-1 of this Regulation, during 50 days in 1995. In this case, JJ did not exceed the thirty (30) days of reserved use, nor the sixty (60) days of "walk-in" use provided for in this Regulation. Should JJ wish to reserve and use his unit in excess of the number of days in the year to which he is entitled according to the provisions of this Regulation, whether by reserved use or as a "walk-in," he will be required to pay the prevailing daily rate for travelling guests at the time he uses the same. Should he fail to do so, the operator of the integrated rental program to which JJ's unit belongs must pay the fine set forth in Section 8(b)(3)-1.

(F) Assume that X is an individual who contributes the amount of \$10,000 in cash to Corporation C, which is going to construct a building which will be dedicated to the horizontal property regime for operation as a Condo-

hotel, in exchange for 100 shares of Corporation C issued in their Primary Issue. X's contribution is not an Eligible Investment under the terms of the Act and of this Regulation since the construction of a building for the sale of its units is not an Eligible Business and therefore Corporation C cannot be an Exempt Business.

(G) Assume that X is an individual who contributes the amount of \$10,000 in cash to Corporation C which is going to operate an integrated rental program of units as a Condohotel, in exchange for 100 shares of Corporation C issued in their Primary Issue. In this case X's contribution is an Eligible Investment under the terms of the Act and of this Regulation.

(H) Assume that X is an individual owner of certain lands on which a \$100,000 mortgage was constituted. Said lands have a market value, according to an appraisal acceptable to the Director, of \$200,000, and the mortgage has a cancellation balance of \$40,000. X contributes the lands to Corporation D which is an Exempt Business dedicated to a Tourism Activity, the operation of a Hotel, in exchange for 100 common shares of Corporation D issued in their Primary Issue and said lands are going to be used by the Exempt Business to construct a tower of rooms for rent as part of the Hotel. Subject to approval by the Director, the value of X's Eligible Investment in the Exempt Business is \$160,000.

(I) Under the same pattern of facts as the previous example, if the Exempt Business does not use the lands in a Tourism Activity, X's contribution would not be an Eligible Investment under the Act and this Regulation.

In all of the aforementioned examples the results are the same regardless of whether X is an individual, a corporation, a partnership, a trust or an estate.

§2(n)-3. Corporate Stock. The stock in a corporation which is issued in exchange for a contribution in cash or in lands shall be common, preferred, or preferred convertible to common stock. A contribution in cash or in lands which is made in exchange for stock in a corporation with rights so restrictive that they are nothing more than evidence of the corporation's debt shall not be considered an Eligible Investment. Likewise, any contribution made to a partnership, whether in lands or in cash, shall be in exchange for an interest with full rights in said partnership and not in exchange for an interest with rights so limited that it is nothing more than evidence of the partnership's debt. The Director shall be empowered to determine on a case-by-case basis that a specific contribution does not comply with the requirements of Eligible Investment hereunder.

§2(n)-4. Eligible Investment; Condohotels. Only the amount in cash which is contributed to purchase a unit in a Condo-hotel shall be taken into consideration in order to determine the value of an Eligible Investment made in a Condohotel.

Neither the mortgages which encumber the unit, nor the value of a note contributed in exchange for the unit shall be considered as part of the value of the Eligible Investment.

§2(n)-5. Example. Investor "A" purchases a villa in a tourist complex operated as a Condohotel to be dedicated to the integrated rental program of said complex. "A" purchases the villa for \$100,000, of which he contributes \$20,000 in cash and encumbers the unit with a mortgage for \$80,000 in favor of Bank XX, from which he obtained a mortgage loan in said amount. The Eligible Investment of Investor "A" would be \$20,000.

§2(n)-6. Eligible Investment; Time Share. An investor who contributes cash in exchange for the right to use a unit in a time share program is not making an Eligible Investment under the Act. In the case of time shares, the benefits of the Act correspond, insofar as it qualifies pursuant to the provisions thereof, to the Developer/operator of the project.

§2(u)-1. Developer. Developer means any Investor or any other Person who is affiliated with, owned by or directly or indirectly controlled by said Investor, who is directly or indirectly responsible for the construction, development or administration of the Tourism Project or of the Exempt Business. The term Developer shall include for all purposes of the Act, the Developer's spouse. The Government of the Commonwealth of Puerto Rico shall under no circumstances be considered a Developer for purposes of the Act.

An Investor who purchases a unit in a Condohotel to dedicate it to the integrated rental program shall be, as is any other Developer, subject to the provisions regarding recapture of Articles 5(d)(3) and 5(d)(5) of the Act and its corresponding sections herein.

§2(r)-1. Primary Issue. The criterion to determine whether a contribution to an Exempt Business shall be considered to be made in its Primary Issue of stock or partnership interests shall be if there is a contribution of additional capital to said business, as opposed to merely replacing already existing capital. Investors who acquire stock or a partnership interest from an underwriter, or from a public corporation of the Government of Puerto Rico who acquired said shares or interest in their initial offering to complete the balance of the capital investment required to close the financing for a Tourism Project, shall be considered to have acquired their stocks or interest in their Primary Issue for purposes of the credits provided in Sections 5(a) and 5(e) of the Act.

§3(a)(1)(B)-1. Distribution of Tourism Development Income; Taxation. Distributions of Tourism Development Income shall be subject to taxation only once in the distribution chain. Exempt Businesses which also operate businesses that are not a Tourism Activity under the Act, such as, for example, a casino, shall maintain separate books to determine which distributions qualify as distributions from Tourism Develop-

ment Income and which distributions do not, for which reason they shall be subject to taxation more than once in the distribution chain. Tourism Investment Capital Funds which are stockholders in an Exempt Business shall distribute to their Participants the funds stemming from any distribution which the Exempt Business has made within thirty (30) calendar days from receipt thereof. References to corporations or partnerships in Article 3(a)(1)(B) of the Act are illustrative and shall be interpreted to include Special Partnerships constituted pursuant to Supplement P of the Income Tax Act of 1954, in which case the exemptions provided by the Act shall flow through to the partners of the Special Partnership.

§3(a)(1)(B)-2. Examples. (i) Corporation X is an Exempt Business operating in Puerto Rico. Its Tourism Activity is the operation of a Hotel. Corporation X distributes dividends to its stockholders, Corporation Y, special partnership Z, Tourism Investment Capital Fund W and individuals A and B. For all of the stockholders of Corporation X, with the exception of the special partnership and the Fund, it will be understood that the aforementioned distribution was the first distribution, for which reason they will pay taxes on 10% of the value of the dividends received. The special partnership shall not pay taxes since by operation of law special partnerships are not taxable entities. In the case of the special partnership the distribution of Corporation X to special partnership Z shall not be considered as the first distribu-

tion, but the partners shall pay taxes immediately since according to the provisions of Supplement P of the Income Tax Act of 1954 it is understood that the Partners received the distribution as soon as the special partnership received it. The Fund shall not pay taxes on the dividends received, since by operation of Article 18 of the Act, the Fund is exempt from the payment of all taxes. Thus, in the case of the Fund, the distribution of Corporation X to the Fund shall not be considered as the first distribution. The stockholders of Corporation Y shall not pay taxes when they are distributed the dividends received from Corporation X since the Corporation paid taxes on the dividends in the first distribution. As mentioned previously, the partners of special partnership Z shall pay taxes in accordance with the provisions of the Income Tax Act. The Participants in Fund W shall pay taxes on 10% of the distribution made by the Fund of the dividends received from Corporation X as long as such distribution is in excess of the adjusted base which the Participant has in his participation in the Fund. Any subsequent distribution made by a corporate Participant in the Fund to its own stockholders shall not be a taxable event.

§3(a)(1)(C)-1. Sale or Exchange. For purposes of the Act, the term "sale or exchange" shall be deemed to include the redemption of corporate stock or interests in a partnership, including special partnerships, and the process of total or partial liquidation of a corporation or partnership. In order

for the provisions of Article 3(a)(1)(C) of the Act to be applicable, the property must continue to be dedicated to a Tourism Activity for a period of not less than twenty-four (24) months after the sale or exchange. However, in cases where said requirement is not met, the Director shall consider the profits or losses to be exempt under the following circumstances: (i) the sale of stock by minority stockholders (for example, a stockholder who owns less than 5% of the stocks issued and outstanding) or interests in a partnership with limited rights to participate in the administration thereof; or (ii) when the circumstances which gave rise to the property not continuing to be dedicated to a Tourism Activity reveal that there was a genuine effort on the part of the buyers to continue dedicating it to a Tourism Activity. In any sale or exchange of stock, interests in partnerships, interests in joint ventures or of all of the assets dedicated to a Tourism Activity of an Exempt Business, the portion which will be exempt in like proportion to the Tourism Development Income of the Exempt Business shall be that which comes from the assets dedicated to the Tourism Activity.

In order for the profits or losses derived from the sale or exchange to be considered as originating from an exempt activity, the requirement that the assets continue to be dedicated to a Tourism Activity shall be applicable independently of whether it is a sale or exchange of stock, interests in partnerships, interests in joint ventures, or of all of the

assets of the Exempt Business. A grantee which has profits derived from the sale or exchange of assets which are not dedicated to a Tourism Activity, such as, for example, a casino, shall deduct the same from the product of the sale to determine the exempt portion.

The exemption to which the grantee shall be entitled in cases of sales or exchanges shall not depend on whether or not the grantee utilized its right to not be covered by the income tax exemption (flexible tax exemption) of Article 3(a)(1)(D) of the Act during the year in which the sale or assignment takes place. Thus, the income generated from the sale of all of the assets of a Tourism Activity, made in a year in which the grantee owner of said Tourism Activity utilized the benefits of the flexible tax exemption, shall be exempt in the same measure as they would be if the grantee had not utilized the aforementioned benefits. The benefits of tax exemption in the profits derived from the sale or assignment of the stock or interests in the Exempt Business, however, shall only be available for a period of ten (10) years from the date of commencement of the Tax Exemption Concession for purposes of payment of income taxes.

§3(a)(1)(C)-2. Example. Corporation CH owns and operates the CH Hotel and Casino and, in 1994 obtained a Tax Exemption Concession under the Act for the operation of the Hotel. According to the terms of the Concession, CH's hotel operations are 90% tax exempt. In the year 2002, the Corporation

sells the CH Hotel and Casino. The basis of Corporation CH is 100x in the Hotel and 100x in the Casino. The sales price is 800x, of which 500x come from the assets of the Hotel and 300x come from the assets of the casino. From the 600x profit which the Corporation generated in said sale, 400x, which constitute the profits from the sale of the Hotel shall be 90% tax exempt. The 200x stemming from the sale of the casino shall be fully taxable.

§3(a)(1)(D)-1. Flexible Tax Exemption. Income tax exemption may be used flexibly, in such a way that in any year after the approval of a Concession and in which the income tax exemption has commenced, the Exempt Business may elect not to be covered by the income tax exemption for that year. The year in which it is not covered by the exemption shall not be considered as part of the total ten (10)-year period of income tax exemption to which the Exempt Business is entitled.

The Exempt Business shall notify the Secretary of the aforementioned election by notice therefor with the income tax return for that particular year. Such notice and election shall be irrevocable for that tax year.

The use of that election shall in no manner affect the other exemptions granted by the Act.

§3(a)(1)(D)-2. Examples. (i) Assume that Corporation X is an Exempt Business which received a Concession for the benefits of the Act effective as of January 1, 20X0 and that the income tax exemption commenced as of that same date. Corporation X

files its income tax return on the basis of the calendar year. For tax years 20X0, 20X1, 20X2 and 20X3 Corporation X used its income tax exemption. At the time it filed its return for tax year 20X4, Corporation X notified the Secretary that it was using the flexible tax exemption granted by Article 3(a)(1)(D) of the Act. Again in 20X5 Corporation X used its income tax exemption. For purposes of the Act, Corporation X has used five (5) of its ten (10) tax exemption years.

§3(a)(1)(G)-1. Carryover of Losses of an Exempt Business; Meaning of Similar Nature. The losses of an Exempt Business may be carried over to future years pursuant to the provisions of the Income Tax Act, with the exception that a net loss may only be deducted against income of a similar nature, except in cases of special partnerships, in which case nothing provided herein shall in any way limit the right of its partners under the Income Tax Act to take a deduction for their share of the loss of the special partnership against income from other sources subject to the limitations of said act. Similar nature shall be deemed to mean that the loss generated in a year in which the election of Article 3(a)(1)(D) is in effect may be deducted only against profits generated in a year in which the election of such Article was used, and that losses generated in a year in which use was made of the tax exemption provided by the Act may only be used against Tourism Development Income generated in a year in which such exemption is used.

Losses which are carried over by the Exempt Business according to the Income Tax Act, regardless of their nature, may be used against income generated by the sale or exchange of the Exempt Business, according to the provisions of Article 3(a)(1)(C) of the Act and the corresponding sections of this Regulation.

Subject to the provisions regarding carryover of losses of the Income Tax Act of 1954, losses generated by the Exempt Business in activities which would qualify as a Tourism Activity under the Act prior to the date of commencement of its Tax Exemption Concession may only be used: (a) against income from any kind generated prior to the commencement of the Tax Exemption Concession, (b) against Tourism Development Income in the years in which the Exempt Business makes use of the flexible exemption of Article 3(a)(1)(D) of the Act, or after the Concession's expiration date, and (c) against income which is not Tourism Development Income at any time during the Tax Exemption Concession.

Losses generated by an Exempt Business resulting from the operation of a casino may only be used against income which is not Tourism Development Income at any time during the Tax Exemption Concession.

§3(a)(1)(G)-2. Examples. (i) Assume that Corporation X is an Exempt Business which received a Concession for the benefits of the Act effective as of January 1, 20X0 and that the income tax exemption commenced on that same date. Corporation X

files its income tax return on the basis of the calendar year. For tax years 20X0, 20X1 and 20X2, Corporation X used the benefits of flexible tax exemption since it incurred losses of \$20,000 in each of those years. For tax year 20X3, the Corporation generated Tourism Development Income of \$60,000. In order to use the loss of \$60,000 generated in years 20X0-20X2 against the Tourism Development Income of year 20X3, Corporation X must again make the election of Article 3(a)(1)-(D) of the Act.

(ii) Assume that Business Y, a corporation, generated losses of \$25,000 during tax year 20X0. On January 1, 20X3, Business Y obtains a Tax Exemption Concession which commencement date shall be January 1, 20X4. The losses of what is now Exempt Business Y generated in tax year 20X0 may only be used against income generated: (a) prior to January 1, 20X4, (b) in any year in which Exempt Business Y decides to adopt the benefits of flexible tax exemption of Article 3(A)(1)(D) of the Act, or, (c) subject to the provisions on carryover of losses of the Income Tax Act, against income generated after the Tax Exemption Concession approved on January 1, 20X4 expires or otherwise ceases to be in effect.

§3(a)(4)(B)-1. Excise Tax Exemption; Certificate of the Director Confirming the Genuine Effort.

(a) The Exempt Business shall apply in writing to the Director for issuance of the certificate, accompanying

a copy of the documents which certify that the articles shall be used in the development, organization, construction or in the course of the operation of the Tourism Activity object of the Concession and not in any other related operation of the petitioner. Among the documents which may be included to comply with this requirement are purchase orders, invoices, blueprints, professional certifications, shipping acknowledgements and other similar documents.

(b) The application shall be filed at the Office of the General Counsel of the Tourism Company.

(c) All documents shall clearly state the date, order number, petitioner, supplier, nature and destination of the articles, price, units and any other information which permits its identification and determination of eligibility.

(d) The Director shall request from the Exempt Business any evidence he deems necessary regarding the efforts made to acquire the articles imported in Puerto Rico, regarding their use in the Tourism Activity object of the Concession, and regarding the economic reasons which justify their being imported into the Island, considering the quality, amount, price and availability.

§3(a)(4)(B)-2. Certificate of Confirmation; Internal Procedure; Right to Reconsideration.

(a) The Office of the General Counsel shall verify that all of the documents have been filed as required,

shall evaluate the applications in consultation with other areas of the Tourism Company and shall prepare the corresponding certificate for signature by the Director or authorized representative. In cases where personnel from said Office determine that the petitioner must submit additional documents to those already submitted, it shall so inform the petitioner and shall provide a reasonable period of time within which said documents must be submitted. Should the petitioner fail to submit the documents required within the term set forth, it shall be deemed that the petitioner's application for a certificate of confirmation has been withdrawn.

(b) Certificates of confirmation shall be numbered consecutively and a file shall be maintained classified by entity or Exempt Business, in which the documents relative to each certificate shall be included.

(c) In cases in which the Certificate of Confirmation is not issued, the Exempt Business may request reconsideration within the term of fifteen (15) days and present additional evidence which justifies the issuance of the certificate.

(d) The certificate of confirmation shall be issued to the Secretary, Attention of the Director of the Excise Tax Bureau of the Department of the Treasury, with a copy to the petitioner.

§3(a)(4)(B)-3. Notices; Regular Mail. Unless indicated otherwise for a specific procedure, all notices which are

required by the procedures governed by this Regulation shall be made by regular mail, unless the parties request otherwise.

§3(b)(1)-1. Date of Commencement of the Tourism Activity.

The date of commencement of the Tourism Activity for Exempt Businesses shall be determined by the Director, with the recommendation of the Secretary.

§3(b)(1)-2. Date of Commencement; Ruling; Procedures.

(a) The date of commencement of the Tourism Activity shall be: (i) the date of the first payroll of the personnel dedicated to training; (ii) the date on which the Exempt Business accepts its first travelling guest or admits the first paying visitor to its premises, or (iii) when the establishment of the date of commencement of the Tourism Activity, as provided herein, results in a substantial prejudice due to circumstances completely beyond the control of the Exempt Business, any other date determined by the Director. The term "circumstances completely beyond the control of the Exempt Business" includes, but is not limited to, strikes, catastrophes or similar circumstances which may result in substantially interrupting the training of personnel or the opening date of the Exempt Business. In these cases, the date of commencement may be postponed while the period of interruption persists. Such period of interruption shall not exceed 12 months from the date indicated in subparagraphs (i) or (ii) hereof.

The Exempt Business shall give immediate notice in writing, and will include all relevant information regarding the occurrence of the interruption, as well as its termination, to the Director and to the Secretary. The Exempt Business shall establish that the interruption was not caused by any act of its own.

(b) If the application is filed after the Exempt Business has commenced its Tourism Activity, the date of filing shall be considered to be the date of commencement of the Tourism Activity.

§3(b)(1)-3. Extensions to the Tax Exemption Concession under the Act. The date of commencement of the extensions to the tax exemption Concession shall be:

(a) The day following the expiration date of the Concession for which the extension is requested.

(b) The day chosen by the grantee, prior to the expiration date of the Concession for which the extension is requested, provided that the grantee relinquish the remaining period of the latter.

§3(b)(2)-1. Postponement of the Date of Commencement of an Exemption. Once an application for a Concession for the benefits of the Act has been approved, the exemptions granted by the Act shall commence to govern as of the date mentioned in Article 3(b)(2) of the Act, except if otherwise elected. Each exemption granted by the Act shall have a different commencement date and each may be postponed at the election of

the Exempt Business until it is more favorable. Exemptions may not be postponed beyond thirty-six (36) months after the date of commencement provided for by the Act.

§3(b)(2)-2. Postponement of the Date of Commencement of an Exemption; Notice. Exemptions granted by the Act may be postponed by notice filed with the Secretary, the Executive Director of the Municipal Income Collection Centers (known in Spanish by the acronym "CRIM") and the Director in conjunction with an application for the benefits of a Concession under the Act, or thirty (30) days prior to the date for filing any return (including extensions) of (i) income taxes, (ii) property taxes, or (iii) municipal license or excise taxes.

§3(b)-3. Contents of the Notice. When the notice of postponement of the exemptions granted by the Act is included with an application for a Concession, the same shall be in the form of an attachment thereto which shall contain the following information:

1. Name and address of the Exempt Business
2. Type of exemption which the Exempt Business wishes to postpone and the period during which it wishes to postpone the exemption.

§3(b)-4. Notice After the Date of the Concession; Sworn Statement. The notice for postponement of the exemptions granted by the Act made subsequent to the date of the Concession, shall be made through a sworn statement which shall contain the following information:

1. Name and address of the Exempt Business
2. Date of the Concession
3. Statement to the effect that the exemptions have not been previously postponed for a period exceeding thirty-six (36) months and that the postponement desired will not result in a postponement beyond the period of thirty-six (36) months.
4. Type of exemption which the Exempt Business wishes to postpone and the period during which it wishes to postpone the exemption.

The Director shall issue an order which indicates the dates of commencement of the exemptions. The order indicating the dates of commencement of the exemptions shall accompany any tax return which must be filed with respect to the exemptions granted.

§4(b)-1. Application for Extension of the Exemption Period.

The application for the extension of the exemption period shall be made pursuant to Sections 3(b)(2)-2, 3(b)(3), and 3(b)(4) hereof.

§4(b)-2. Deadline for Filing the Application for Extension.

The application for extension shall be filed by the Exempt Business on or before the deadline under the Income Tax Act for filing the income tax return for the last year during which it will enjoy income tax exemption.

§5(a)-1. Tourism Investment Tax Credit; Operation. Subject to the different limitations imposed by the Act and this Regulation, the tourism investment tax credit shall be available for use solely and exclusively against any tax obligation imposed by the Income Tax Act of 1954, as amended. Thus, a corporation which enjoys a 90% Tax Exemption Grant under Act No. 8 of January 24, 1987, as amended, may apply a tourism investment tax credit in its return for tax year 1993 against its income taxes of four point five percent (4.5%) imposed by the Income Tax Act (the maximum corporate rate of forty-five percent (45%), multiplied by the 90% exemption), but not against the point five percent (.5%) tax imposed by said Act No. 8 of January 24, 1987, as amended, for corporations which generate more than \$1 million in industrial development income.

In the case of corporations and other juridical persons who are Grantees under the Act, the tourism investment tax credit belonging to the juridical person may only be used against the tax liability of the juridical person itself and not against the tax liability of its stockholders or partners as would be, for example, the withholding tax according to Section 143 of the Income Tax Act of 1954, as amended. In these cases, the juridical person could, however, transfer the tourism investment tax credit to its stockholders or partners pursuant to the provisions of Article 5(f) of the Act and the corresponding sections of this Regulation for the stockholders

or partners to use it against the aforementioned withholding tax.

A taxpayer who is entitled to a tourism investment tax credit and does not use such credit against its tax liability nor assigns, sells or otherwise transfers all or part thereof shall not, under any circumstances, have the alternative of requesting from the Department of the Treasury that it be paid in cash for the amount of the credit which was not used. However, when a tourism investment tax credit is used against a withholding tax, such as, for example, the taxes imposed by Sections 11A, 11B and 11C of the Income Tax Act of 1954, the taxpayer may opt for being credited with the tourism investment tax credit first, and being reimbursed for the excess of the taxes withheld after applying the tourism investment tax credit used.

To take a tourism investment tax credit, an Investor or Participant must file, together with the income tax return, a copy of the sworn statement required of the Exempt Business by Article 5(c) of the Act and the corresponding section of this Regulation, as well as the certificate mentioned in Sections 5(a)-3 or 5(a)-4, or, in the case of the Condohotels, a copy of the Tax Exemption Concessions mentioned in Section 5(a)-5 hereof, as the case may be.

§5(a)-2. Tourism Investment Tax Credit; Requirements for Availability. The tourism investment tax credit shall be available to be taken during the tax year prior to the year in

which the Eligible Investment was made for all Eligible Investments which are made prior to the filing date for the income tax return of the Investor or Participant for said year, including extensions. Furthermore, in order to take such tourism investment tax credit, it shall be necessary: (i) that the transaction whereby the Exempt Business obtained the necessary financing to carry out the Tourism Project have been completed, (ii) that Sections 5(a)-3, 5(a)-4, or 5(a)-5 hereof, as the case may be, be complied with, and (iii) except in situations in which the Director determines that the best interests of Puerto Rico require otherwise, that the Eligible Investment be made after the date of effectiveness of the Act.

§5(a)-3. Tourism Investment Tax Credit. Right to Take the Tourism Investment Tax Credit in Cases in which One of the Investors is a Tourism Investment Capital Fund. Notification Procedure. In the case of Tourism Projects in which a Tourism Investment Capital Fund participates, the procedure whereby the Investors and Participants who are entitled to take tourism investment tax credits are notified that they may take such credits shall be as follows:

- (i) The agent in charge of the escrow account where the funds belonging to the Tourism Investment Capital Fund are deposited ("escrow agent") shall disburse said funds to the financial entity which provided the loan to complete the financing for the Tourism Project or, in cases where a bond

issue has been made, to the trustee in charge of proceeds.

(ii) Once said funds have been disbursed, the escrow agent shall certify by certified mail or messenger, return receipt requested, to the administrator of the Tourism Investment Capital Fund and to the Tourism Project Developer that the funds were disbursed.

(iii) The administrator of the Tourism Investment Capital Fund and the Tourism Project Developer, in turn, shall execute a joint sworn statement, which they shall send by certified mail or messenger, return receipt requested, to all of the Participants of the Tourism Investment Capital Fund and to all of the other Investors in the Tourism Project. The joint sworn statement shall include:

(1) a statement from the Developer to the effect that the sum of (a) the capital investments made in the Exempt Business, (b) the capital invested through the Tourism Investment Capital Fund organized for the project, and (c) the funds originating from the loan taken to complete the financing, total 100% of what at that time is considered to be the total cost of the Tourism Project;

- (2) a statement from the escrow agent to the effect that it disbursed said funds to the financial entity which provided the loan or to the trustee in charge of the proceeds; and
- (3) the total amount of tourism investment tax credit available for the Tourism Project, and an itemization which identifies the amount to which each of the Investors and/or Participants is entitled according to the distribution agreed to between the Developer and the administrator of the Fund, and notified to the Investors and Participants pursuant to the provisions of Section 5(c)-1 hereof.

The joint sworn statements shall also include a copy of the aforementioned certificate issued by the escrow agent. A copy of the joint sworn statement shall be sent by certified mail, in turn, to the Executive Director of the Tourism Company and to the Secretary of the Treasury.

- (iv) The right to take the tourism investment tax credit arises when each Investor/Participant receives the joint sworn statement from the administrator of the Fund and the Tourism Project Developer, accompanied by the certification from the escrow agent. Each Investor or Participant, including the Tourism Project Developer, shall

attach a copy of the joint sworn statement issued by the administrator of the Fund and the Tourism Project Developer, as well as a copy of the certification provided by the escrow agent, with its income tax return for each year in which he utilizes his tourism investment tax credit. Said return shall also contain the following information: (1) the total tourism investment tax credit to which the taxpayer is entitled as a result of its Eligible Investment; (2) the amount of said tourism investment tax credit which was previously used by the Investor/Participant and the tax year in which it was used; (3) the amount of the tourism investment tax credit available, and (4) the amount of the tourism investment tax credit to be taken in that tax year.

§5(a)-4. Tourism Investment Tax Credit. Right to Take the Tourism Investment Tax Credit in Cases in which there is no Participation by a Tourism Investment Capital Fund. In cases where there is no participation whatsoever by a Tourism Investment Capital Fund, the right of the Developer or any other Investor to take his tourism investment tax credit will arise when the Developer, together with the financial institution which provides the financing for the Tourism Project, or, in cases in which there has been a bond issue, the trustee in charge of proceeds, certify that 100% of what at that moment

appears to be the total cost of the Tourism Project has been raised through:

- (a) capital investments,
- (b) legally binding commitments to make capital investments on the part of agencies of the Commonwealth of Puerto Rico, and
- (c) financing through private financial institutions or agencies of the Commonwealth of Puerto Rico,

and that all of the pertinent contracts have been executed to establish that the commitments made are legally binding. The process whereby certification is made to the Investors who are entitled to take the tourism investment tax credit shall be as follows:

- (i) the financial institution which provided the financing for the Tourism Project or, in cases in which there has been a bond issue, the trustee in charge of proceeds, shall certify to the Developer the amount of money which has been raised through capital investments and financing.
- (ii) the Tourism Project Developer, and an officer of the financial institution, or, in cases in which there has been a bond issue, the trustee in charge of proceeds, in turn, shall execute a joint sworn statement, which shall be sent by certified mail or messenger, return receipt requested, to all of

the Investors in the Tourism Project. The joint sworn statement shall include:

- (1) a statement by the Developer to the effect that the sum total of the capital investments made in the Exempt Business, and the funds originating from the loan taken or from the bond issue made to complete the financing, equals 100% of the total cost of the Tourism Project at that time, and;
- (2) the total amount of tourism investment tax credit available for the Tourism Project, and an itemization which identifies the amount to which each of the Investors is entitled, including the Developer.

The joint sworn statements shall also include a copy of the aforementioned certificate issued by the financial institution which provided the financing. A copy of the joint sworn statement shall be sent by certified mail, in turn, to the Executive Director of the Tourism Company and to the Secretary of the Treasury.

- (iii) The Investors in the project may begin taking their tourism investment tax credits when they receive the sworn statement from the Tourism Project Developer and from the official of the financial institution, accompanied by the latter's

certification. Each Investor, including the Tourism Project's Developer, shall attach a copy of the sworn statement, as well as a copy of the certification provided by the financial institution, to his income tax return for the years in which he makes use of his tourism investment tax credit. Said return shall also contain the following information: (1) the total tourism investment tax credit to which the taxpayer is entitled as a result of his Eligible Investment; (2) the amount of said tourism investment tax credit which was used previously by the Investor and the tax year in which he used the same; (3) the amount of the tourism investment tax credit available, and (4) the amount of the tourism investment tax credit to be taken in that tax year.

§5(a)-5. Tourism Investment Tax Credit. Right to Take the Tourism Investment Tax Credit in the Case of Units in a Condohotel. In the specific case of units in a Condohotel, only those owners who acquire their unit directly from the Developer in the first purchase and sale transaction of the unit will be entitled to take the tourism investment tax credit and the credit for loss of Article 5(e) of the Act. The right of the purchaser of the unit to take the tourism investment tax credit arises when he receives from the Director his Tax Exemption Concession, after complying with

the requirements set for in the last paragraph of Section 9(c)-1(a) of this Regulation. However, said right shall be retroactive to the date of filing of the application for the Concession. The provisions of this section shall have no effect whatsoever on the right of an owner of a Condohotel to assign, sell, or otherwise transfer his tourism investment tax credit pursuant to the provisions of Article 5(f)-1 of the Act and the corresponding sections of this Regulation.

§5(a)-6. Tourism Investment Tax Credit; Limitations. The tourism investment tax credit is limited to 50% of the Eligible Investment made by the Investor or Participant. During the first tax year when there is a right to take the tourism investment tax credit, that is, the tax year in which the Exempt Business closed its financing and complied with the requirements of Sections 5(a)-3, 5(a)-4, or 5(a)-5 hereof, as the case may be, no more than half of the tourism investment tax credit available may be taken pursuant to the limitations imposed by the global amount of tourism investment tax credit available for the Tourism Project. In cases in which the Investor/ Participant makes an Eligible Investment after conclusion of the tax year but prior to filing the income tax return for said year, the Investor/Participant may take half of the tourism investment tax credit to which he is entitled in said tax year and the other half in the following tax year.

No Investor or Participant may take a tourism investment tax credit if he has not complied with all of the requirements of Article 5 of the Act and its corresponding sections herein.

§5(a)-7. Tourism Investment Tax Credit; Substitution of Securities in a Fund. No tourism investment tax credit shall be available to any Participant who acquires participations in a Fund, to substitute participations in another Fund which were sold, assigned or transferred in any manner, and with respect to which no profits or losses was acknowledged.

§5(a)-8. Tourism Investment Tax Credit; Tourism Project Developer. A Developer may not be a Participant in a Fund organized for the purpose of making an Eligible Investment in the Tourism Project which the Developer is developing.

§5(a)-9. Tourism Investment Tax Credit; Time Shares. In the case of time shares, the right to the tourism investment tax credit belongs to the Developer/operator of the project, and not to the person who contributes cash in exchange for the right to use a unit for a limited period of time each year. On the other hand, in the case of Condohotels, the owner of each unit shall be entitled to the tourism investment tax credit and the exemptions provided by Article 3 of the Act, while the operator of the integrated rental program shall only be entitled to the exemptions provided by Article 3.

§5(a)-10. Cases in which a Tourism Investment Capital Fund is Not Able to Raise 20% of the Total Cost of the Project. Any Developer who, after making an Eligible Investment of at least

20% of the total cost of the Tourism Project, and obtaining a loan or obtaining funds from a bond issue for an amount equal to at least 60% of said cost, is not able to raise through a Tourism Investment Capital Fund the remaining 20%, may close the entire financing necessary to develop the project with additional financing, either through a bridge loan, or through additional capital investments, for the difference between the Fund's contribution and the remaining 20%.

As in the rest of the cases in which a Fund has been organized, the right to the tourism investment tax credit shall arise when the mechanism set forth in Section 5(a)-3 of this Regulation is complied with.

§5(a)-11. Annual Reports to the Secretary. No later than January 31 of each year, the Director shall send to the Secretary and to the Executive Director of CRIM a list of the natural and/or juridical persons who obtained Tax Exemption Concessions under the Act during the previous year, their social security number, and the amount of the tourism investment tax credit to which they are entitled according to their Concession. Likewise, the Director shall also inform the Secretary of any assignment of tourism investment tax credits of which he has been notified during the previous year.

§5(a)-12. Examples. (i) Taxpayer A is an individual who makes an Eligible Investment in Exempt Business Z on March 15, 20X1. Exempt Business Z closes the necessary financing to complete the Tourism Project on April 14, 20X1. Subject to the

provisions of Sections 5(a)-2 and 5(a)-3, or 5(a)-4 hereof, as the case may be, Taxpayer A is entitled to take half of its tourism investment tax credit in his income tax return for calendar year 20X0.

(ii) Assume the same facts of example (i), but the Exempt Business does not complete its financing until past April 15, 20X1. Unless Taxpayer A receives an extension to file its return for the year 20X0 on a date after the date on which Exempt Business Z closed its financing and complied with the provisions of Sections 5(a)-2 and 5(a)-3 or 5(a)-4 hereof, Taxpayer A may not take the tourism investment tax credit on his 20X0 tax return.

(iii) Taxpayer A is an individual who made an investment in a Tourism Investment Capital Fund on March 15, 20X1. On April 15, 20X1, the escrow account in which the monies contributed to the Fund were deposited was dissolved because the Exempt Business did not close its financing on or before that date. Taxpayer A shall not be entitled to a tourism investment tax credit.

(iv) Assume the same facts as example (iii) but the Fund requests and is granted an extension to make the Eligible Investment, and on May 15, 20X1, the Exempt Business closes its financing and on that same date the Fund makes the Eligible Investment in the Exempt Business. Subject to the provisions of Sections 5(a)-2 and 5(a)-3 hereof, if Taxpayer A requested and was granted an extension to file his

income tax return for the year 20X0, he could take the tourism investment tax credit on his return for the year 20X0.

(v) Assume the same facts of example (iv) with the exception that the participation which Taxpayer A bought in the Fund was made to substitute a participation in another Fund which he sold previously and over which he did not recognize any gains or losses. Taxpayer A does not have, under any circumstances, a right to a tourism investment tax credit.

(vi) Taxpayer A, who is an individual, is the Developer of Tourism Project MM. Fund DD is organized to make an Eligible Investment in Tourism Project MM. Taxpayer A is prohibited by operation of the Act from participating in Fund DD.

(vii) Partnership "A" makes an Eligible Investment of \$20 million to develop a Tourism Project whose total cost will be \$100 million. "A" obtains a commercial loan of \$60 million to finance said project. The Tourism Investment Capital Fund organized to make an Eligible Investment of \$20 million in "A's" Tourism Project is only able to raise \$10 million. "A" would have the option of structuring the financing of his project in such a way that the Fund only invests the \$10 million which it raised, and making up the difference through another capital investment or another commercial or government bridge loan of \$10 million, thus

closing the financing for the Tourism Project with the money obtained through said capital investment or loan.

§5(b)-1. Tourism Investment Tax Credit; Carryover of the Credit; Maximum Amount to be Taken in a Specific Year. During the first tax year in which one is entitled to take a tourism investment tax credit, only half of the credit generated by the Eligible Investment may be taken.

§5(b)-2. Example. Investor YY purchases a share in Tourism Investment Capital Fund HH which generates for him a tourism investment tax credit of \$6,000. The Exempt Business in which Fund HH makes its Eligible Investment closes its financing and complies with the requirements of Section 5(a)-3 of this Regulation on April 12, 1994. YY uses the calendar year as its tax year and will file its income tax return for the year 1993 on April 14, 1994. YY may take a tourism investment tax credit of \$3,000 in tax year 1993 and \$3,000 in tax year 1994. If he so wishes, YY may also opt for not taking any tourism investment tax credit during tax year 1993, which will allow him to take the entire tourism investment tax credit (\$6,000) in tax year 1994 or at any time after said date.

§5(b)-3. Tourism Investment Tax Credit; Credits Originating from Different Transactions. In cases in which an Investor who is entitled to a tourism investment tax credit ("itc") makes an Eligible Investment which generates another itc, the second itc generated may be used together with the first one, but both tourism investment tax credits shall maintain their

individuality for purposes of determining the maximum amount which may be used in a specific year pursuant to the provisions of Article 5 of the Act and of this Regulation.

§5(b)-4. Examples. (i) Investor JJ makes an Eligible Investment in the year 20X1 which generates for him a tourism investment tax credit ("itc-1") amounting to \$50,000. During the years 20X1 through 20X3, JJ uses the carryover set forth in Article 5(c) of the Act and does not use his tourism investment tax credit. During the year 20X4, JJ makes another Eligible Investment which generates for him a tourism investment tax credit of \$20,000 ("itc-2"). The financing for the project in which JJ made the second Eligible Investment closed, and the corresponding documentation was issued, during that same year 20X4. The maximum credit which JJ will have available to use in any year after tax year 20X4 shall be \$60,000 [\$50,000 from itc-1 and \$10,000 from itc-2].

§5(c)-1. Tourism Investment Tax Credit; Distribution; Reports. The global amount of tourism investment tax credit which will be available per Tourism Project to be taken by Investors and Participants shall be equal to 10% of the total cost of the Tourism Project, as said cost is determined by the Director as part of the procedure for granting the exemption, or 50% of the amount invested in cash as Eligible Investment in the Tourism Project, whichever is less.

The value of the land contributed to an Exempt Business, although it is an Eligible Investment, shall not be included

when computing the amount of cash contributed to the Exempt Business.

As a general rule, and except in situations where the Director determines that the best interest of Puerto Rico require otherwise, the calculation of what constitutes the total cost of the Tourism Project shall include: (i) all of the expenses and disbursements incurred by the Exempt Business, including the salaries paid to their employees, in the acquisition of the land, construction, outfitting, marketing up to the moment of its opening and the expenses for the opening ceremony of a New Business; (ii) the capitalized interest on the financing obtained during the construction period and during the first six (6) months (or any additional period as required by the Tourism Development Fund or the Hotel Development Corporation as a condition for the financing), after commencement of operations of a New Business, that is, from the time the New Business opens its doors to the public; (iii) the expenses incurred in the substantial renovation or expansion of an Existing Business; (iv) the expenses related to the issuance of debt or to raise capital for the Exempt Business; (v) any reserve account required by the Tourism Development Fund as a condition to guarantee the financing for the Exempt Business, and (vi) any contribution made by the Government of Puerto Rico in exchange for stock or an interest in the Exempt Business through its agencies, instrumentalities, or public corporations for purposes of

designing and constructing infrastructure projects for the benefit of the Exempt Business.

On the other hand, said calculation of the total cost of the Tourism Project shall exclude, as a general rule and except in situations where the Director determines that the best interests of Puerto Rico require otherwise: (i) the money which has been invested prior to the date of effectiveness of the Act, and (ii) the money which has been invested prior to meeting with the officers designated by the Tourism Company to discuss the merits of the proposed project (pre-application conference).

Under no circumstances shall the following be considered in the computation of what constitutes the total cost of the Tourism Project: (i) the money used to acquire facilities which have been dedicated to a Tourism Activity in a way that could not be categorized as "incidental" at any time during the thirty-six (36) months prior to the filing of an application for a Concession under the Act, and (ii) the estimated cost of the time invested by the Developer or by any stockholder of the Exempt Business.

The global amount of tourism investment tax credit may be distributed among Investors and Participants in the manner in which they decide, as long as they comply with the provisions of Article 5(a) of the Act to the effect that no Investor or Participant may take a tourism investment tax credit which exceeds 50% of its cash investment. However, when one of the

Investors or Participants is the Government of Puerto Rico, the proportion of tourism investment tax credit to which it will be entitled as a result of said distribution shall not be less than the proportion of its Eligible Investment compared to all of the Eligible Investments made for the Tourism Project. In cases in which the Investors and/or Participants in a Tourism Project wish to depart from said rule they shall obtain prior written approval from the Director, the Secretary and the President of the Government Development Bank.

The Exempt Business shall inform the Investors, Participants, the Tax Exemption Enforcement Division of the Department of the Treasury and the Director of such distribution on or before the date on which the Exempt Business files its income tax return for its first year of operations, including any extension of time to file the same. Such notice shall be made through sworn statement which shall contain the following information:

1. Name and address of the Exempt Business.
2. Name and address of the Tourism Project Developer.
3. Name, address, social security number and the amount of the Eligible Investment of all of the Investors and Participants of the Exempt Business.

4. Distribution in percentages and amount of the tourism investment tax credit granted to the Investors and to the Participants.
5. Total cost of the Tourism Project as approved by the Director in the Concession.
6. Global tourism investment tax credit available for the Tourism Project, as computed by the Exempt Business.
7. Statement to the effect that financing for the Tourism Project has been obtained, accompanied by a letter from the financial institution which provided the funding certifying that the same has already been granted, and the amount and terms thereof.

\$5(c)-2. Examples. (i) Exempt Business RR develops a Tourism Project estimated at \$100 million. The Tourism Project will not use existing facilities. The Exempt Business attracts Investors who contribute \$10 million in cash, and other Investors who contribute \$10 million in land. These investments are made after the date of effectiveness of the Act and after filing an application for a Concession thereunder. The Exempt Business causes the organization of a Fund so that upon closing, it makes an Eligible Investment of \$20 million (the maximum amount which the Fund may contribute pursuant to Article 11(b) of the Act). The global tourism investment tax

credit available for the Investors and Participants is \$10 million, computed as follows:

Total cost of the Tourism Project	\$100 million
10% of the total cost	<u>\$ 10 million</u>
Cash contributed to the Exempt Business by the Investors and Participants	\$ 30 million
50% of the cash contributed	<u>\$ 15 million</u>
Global tourism investment tax credit available	<u>\$ 10 million</u>

Continuing with the example, Exempt Business RR notifies the Investors, Participants, the Secretary and the Director that the tourism investment tax credit shall be distributed as follows:

Investors	0%
Participants	100%

The Participants will have available \$10 million of tourism investment tax credit which is 50% of their Eligible Investment of \$20 million.

(ii) Corporation BB will purchase an existing Hotel for \$40 million in which it is going to make a substantial renovation of \$10 million, in order to be able to qualify for the benefits of the Act. The transaction is carried out after filing an application for a Concession under the Act. Corporation BB makes a stock offering in which it collects \$50 million. The global amount of tourism investment tax credit available for the Investors is \$1 million, computed as follows:

Total money invested	\$ 50 million
Total cost of the Tourism Project (the substantial renovation)	\$ 10 million
10% of the total cost	<u>\$ 1 million</u>

Cash contributed to the Exempt Business by the Investors	\$ 50 million
Less (-) amount which will not be invested in a substantial renovation or expansion	<u>\$ 40 million</u>

Amount of cash contributed	\$ 10 million
50% of the cash contributed	<u>\$ 5 million</u>

Global tourism investment tax credit available \$1 million

Continuing with the example, Corporation BB notifies the Investors, the Secretary and the Director that the tourism investment tax credit will be distributed as follows:

Investors	100%
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The Investors will have available \$1 million in tourism investment tax credit.

(iii) Special Partnership XYZ develops the XYZ Resort & Casino at a cost of \$100 million. The cash contribution of the partners of XYZ for the development of the Resort & Casino is \$15 million. Of the total \$100 million invested, \$30 million corresponds to the purchase of the lands and legal expenses incurred in said purchase, as well as the acquisition of the necessary permits to operate the complex; \$60 million corresponds to the construction costs, decoration and acquisition of furniture, fixtures and equipment to be used in the Hotel; \$5 million corresponds to the construction and acquisition of all of the furniture, fixtures and equipment to be used in the casino; and \$5 million corresponds to the expenses incurred by the Government of Puerto Rico through

one or more of its agencies, instrumentalities, or public corporations in the construction of an access road to the Hotel and the design and construction of the infrastructure necessary to handle the solid, liquid or other waste generated by the operation of the Hotel. The Government of Puerto Rico, through one or more of its agencies, bureaus or public corporations obtained a 10% interest in Special Partnership XYZ as a result of the aforementioned contribution.

The tourism investment tax credit available for Special Partnership XYZ shall be the lesser amount between: (i) \$9,500,000, which is equal to 10% of the total cost of the Tourism Project [\$100 million less the \$5 million attributable to the construction and acquisition of all of the furniture, fixtures and equipment to be used in the casino]; and (ii) \$10 million, which is equal to 50% of the sum of the cash contributed by the partners of XYZ (\$15 million) and the \$5 million contributed by the Government of Puerto Rico, through one or more of its agencies, bureaus or public corporations.

At the time of the distribution of the \$9,500,000 generated as tourism investment tax credit by the XYZ Resort & Casino, the partners of XYZ must distribute to the Government of Puerto Rico, as a minimum, 25% of said amount, since the Eligible Investment made by the Government of Puerto Rico is one fourth of the total Eligible Investments made for the Tourism Project. Thus, the Government of Puerto Rico would be entitled to a tourism investment tax credit of \$2,375,000.

Should the partners of XYZ wish to distribute to the Government of Puerto Rico a lesser tourism investment tax credit they must, pursuant to the provisions of Section 5(c)-1 hereof, obtain the prior written approval of the Director, the Secretary and the President of the Government Development Bank.

§5(d)-1. Tourism Investment Tax Credit; Basis Adjustment.

The basis of all Eligible Investments shall be determined by the rules of Sections 113 and 344 of the Income Tax Act prior to any adjustment ordered by the Act.

§5(d)-2. Reduction of the Basis. The basis of all Eligible Investments shall be reduced annually by the amount of tourism investment tax credit taken in the Investor's income tax return.

§5(d)-3. Examples. (i) Continuing with the fact pattern of example (i) of §5(c)-2, the Participants may take the tourism investment tax credit of \$10 million in two consecutive years, half in one year and the other half the next year (the example assumes that there will be no carryover of the excess tourism investment tax credits from one year to the next). Therefore, in the first year, after the Participants take \$5 million of tourism investment tax credits, the adjusted base of the Fund's Eligible Investment shall be as follows:

Adjusted Base of the Eligible Investment	\$ 20 million
Adjustment for tourism investment tax credit taken by the Participants	- <u>\$ 5 million</u>
New Adjusted Base	<u>\$ 15 million</u>

§5(d)-4. Annual Report. Annually, on the anniversary of the notification provided for in Article 5(c) of the Act and §5(c)-1 of this Regulation, the Exempt Business shall render a report to the Director and to the Secretary which shall contain the following information:

1. Name and address of the Exempt Business.
2. Name and address of the Tourism Project Developer.
3. Employer Social Security number of the Exempt Business.
4. A statement of the expenses incurred in the development of the project, accompanied by the evidence necessary to certify the same, such as, for example: (a) partial certifications from the civil engineers that the project is in progress; (b) the signed construction contracts; (c) change orders; (d) cost estimates from the suppliers; or (e) any other evidence which the Director deems necessary to certify the expenses incurred.

Said report shall be rendered for three (3) consecutive years. Once satisfied of the certainty of the representations of the Investors and/or Developers to the effect that the total costs of the Project differ from the figures included in the original Tax Exemption Concession, the Director shall proceed to amend said Concession to reflect the real total

cost of the Tourism Project. The total cost of the Tourism Project included in the original Tax Exemption Concession shall remain in effect until the Director amends the same pursuant to the documents submitted to him. The Director shall also redetermine the global tourism investment tax credit available for the Tourism Project and shall notify the Exempt Business.

The Director shall notify the Secretary of any tourism investment tax credits taken in excess by the Investors. The three (3) year period may be extended by the Director at the request of the Exempt Business. The extension granted by the Director may not exceed two (2) years. During the extension period the Exempt Business shall render an annual report in the same manner and with the same information as the report which it rendered during the original three (3) year period. The Exempt Business' petition for the extension granted under Article 5(d) of the Act shall be made through a sworn statement which will contain the following information:

1. Name and address of the Exempt Business.
2. Name and address of the Tourism Project Developer.
3. Reasons why the Exempt Business requires the extension requested.

Should the global tourism investment tax credit computed by the Exempt Business exceed the global tourism investment tax credit computed by the Director, the Exempt Business shall

compute the portion of the excess tourism investment tax credit taken which each Investor Developer must assume as a tax debt. Said division shall be prorated among all of the Investors Developers in the same proportion to the tourism investment tax credit already taken by each Investor Developer. The Exempt Business shall notify, by certified mail, return receipt requested, to the Investor Developers, the Director and the Secretary the excess tourism investment tax credit owed. The tourism investment tax credit taken in excess shall be owed as income tax by the Investor Developers if they were entitled to, and took any portion of the global tourism investment tax credit. The credits taken in excess shall be paid in two (2) installments, the first the year following the expiration date of the three (3) year period, or the three (3) year period plus any extension of time granted by the Director, and the second installment the following year.

Should the global tourism investment tax credit computed by the Director exceed the global tourism investment tax credit computed by the Exempt Business, the Exempt Business shall compute the portion of the excess tourism investment tax credit which has not been distributed. The tourism investment tax credit which has not been distributed shall be distributed in the same proportion as the notice required by Article 5(c) of the Act and §5(c)-1 of this Regulation. If making the distribution in accordance with the aforementioned notice

results in part of the tourism investment tax credit not being able to be taken because the Participants or Investors have reached the maximum of the tourism investment tax credit which each Participant or Investor may take, the Exempt Business shall notify the Director of a new distribution, in the form and manner set forth in §5(c)-1 of this Regulation. The Investors or Participants shall take the remaining tourism investment tax credit after receiving approval from the Director.

§5(d)-5. Examples. (i) Continuing with example (i) of §5(c)-2 and example (i) of §5(d)-3, if after the three (3) year period has elapsed the Director determines that the total investment in the Tourism Project has been \$150 million, the tourism investment tax credit for the Tourism Project would be:

Total cost of the Tourism Project	\$150 million
10% of the total cost	<u>\$ 15 million</u>
Cash contributed to the Exempt Business by the Investors and Participants	\$ 30 million
50% of the cash contributed	<u>\$ 15 million</u>
Global tourism investment tax credit available	\$ 15 million
Credit previously used	\$ 10 million

There is a tourism investment tax credit of \$5 million available to be distributed among the Investors and Participants. However, the Participants received \$10 million in tourism investment tax credit, which is equal to 50% of their \$20 million Eligible Investment. The Exempt Business may then notify the Director of the distribution of the \$5 million

credit to the Investors. The Investors, having contributed \$10 million, may take the total \$5 million credit. The additional \$5 million tourism investment tax credit shall be subject to the same limitation of Article 5(a) of the Act and the corresponding sections of this Regulation in that the Investors may only take up to 50% of the credit during the first year in which they are entitled to take such credit.

(ii) Continuing with example (i) of §5(c)-2, if after the three (3) year period, the Director determines that the total investment in the Tourism Project has been \$80 million, the new global tourism investment tax credit shall be:

Total cost of the Tourism Project	\$ 80 million
10% of the total cost	<u>\$ 8 million</u>
Cash contributed to the Exempt Business by the Investors and Participants	\$ 30 million
50% of the cash contributed	<u>\$ 15 million</u>
Global tourism investment tax credit available	<u>\$ 8 million</u>

There is a credit taken in excess of \$2 million, which shall not be recaptured from the Investors or Developers, since no tourism investment tax credits were originally distributed to the latter, nor from the Participants, since the Participants in a Fund are not subject to recapture of the tourism investment tax credit taken in excess under these circumstances.

(iii) Exempt Business RR has developed a Tourism Project estimated at \$100 million. Investors-Develop-

ers A and B contribute a total of \$20 million (in equal portions) to the Exempt Business. The Exempt Business causes the creation of a Fund so that at the closing, the Fund makes an Eligible Investment of \$20 million (the maximum which the Fund may contribute according to Article 11(b) of the Act). The global amount of tourism investment tax credit available to the Investors and Participants is \$10 million, computed as follows:

Total cost of the Tourism Project	\$100 million
10% of the total cost	<u>\$ 10 million</u>
Cash contributed to the Exempt Business by the Investor-Developers and Participants	\$ 40 million
50% of the cash contributed	<u>\$ 20 million</u>
Global tourism investment tax credit available	<u>\$ 10 million</u>

Continuing with the example, Exempt Business RR notifies the Investors-Developers, Participants, the Secretary and the Director that the tourism investment tax credit shall be distributed as follows:

Investors-Developers	50%
Participants	50%

The Participants shall have available \$5 million of tourism investment tax credit, the Investors-Developers shall have available \$5 million of tourism investment tax credit, and they shall distribute it equally for A and B.

If after the three year period, the Director determines that the total investment in the Tourism Project had been \$80

million, the new global tourism investment tax credit would be:

Total cost of the Tourism Project	\$ 80 million
10% of the total cost	<u>\$ 8 million</u>
Cash contributed to the Exempt Business by the Investors-Developers and Partici- pants	\$ 40 million
50% of the cash contributed	<u>\$ 20 million</u>
Global tourism investment tax credit available	<u>\$ 8 million</u>

There is a credit taken in excess of \$2 million, which will be owed by the Investors-Developers as income taxes since the Participants in a Fund are not subject to recapture of the tourism investment tax credit taken in excess and the Investors-Developers had taken a tourism investment tax credit of \$2,500,000 each. Investor-Developer A shall owe \$1 million (50% of the credit taken in excess) in taxes and Investor-Developer B shall owe \$1 million (50% of the credit taken in excess) in taxes, to be paid pursuant to the Act, that is, both Investor-Developer A and Investor-Developer B shall pay \$500,000 the year in which the three year period expired and \$500,000 the following year.

Had Investors-Developers A and B distributed and taken the \$5 million in tourism investment tax credit computed initially in such a way that A took 20% of the credit generated, and B took 80%, then, at the time it was known that there were \$2 million in tourism investment tax credit taken in excess, A and B would have been required to distribute the tax debt between themselves in that same proportion.

§5(d)-6. Annual Reports in the Case of a Condohotel. The operator of a Condohotel's integrated rental program shall submit annually, before January 31, a sworn statement to the Director and to the Secretary which shall contain the following information:

1. Name, address and employer social security number of the operator of the integrated rental program.
2. Summary of the total number of units participating in the integrated rental program, itemized by month, and indicating the individual number of each unit which participated in the program during that month.
3. Summary by unit indicating the name and address of the owner of the unit, the date of commencement of participation in the program, the date on which it ceased to participate in the program, the number of days in which the unit was reserved and used by the owner, and the number of days in which the owner used the unit without reserving it as provided in §2(n)-1 hereof.

§5(d)-7. Condohotels; Requirements of Maintaining the Unit in the Integrated Rental Program for Ten (10) Years. Any Investor who does not meet the requirement of maintaining his unit(s) in the integrated rental program for ten (10) consecu-

tive years, commencing thirty (30) days after the date of purchase, and for eleven (11) months in each year, shall owe as income taxes the tourism investment tax credit taken in excess. For purposes of determining whether there are any tourism investment tax credits taken in excess, it shall be understood that the Investor is entitled to take as tourism investment tax credit one tenth of the total credit during each year in which the unit is part of the integrated rental program. Thus, the amount which shall be subject to recapture shall be calculated subtracting from the amount of credit taken by the Investor, an amount "X." The amount "X" shall be determined by multiplying the amount of the tourism investment tax credit to which the Investor would be entitled had he maintained his unit in the integrated rental program for the ten (10) years required by the Act, by a fraction which numerator shall be the number of years during which the Investor maintained his unit in the integrated rental program and which denominator shall be ten.

When calculating the balance of the ten (10) year period, fractions of years shall be rounded out to the next year. Any sale, transfer or alienation of the unit by the Investor shall be considered to be a withdrawal from the integrated rental program, except in those cases in which the Tax Exemption Concession is transferred pursuant to the provisions of Article 7(a) of the Act, in which case the subsequent buyer must maintain the unit in the integrated rental program. In

these cases, the seller and the buyer of the unit which shall continue to be dedicated to the integrated rental program shall include in the deed of purchase and sale of the unit a clause indicating that: a) the buyer shall be liable for any amount which must be subsequently recaptured for tourism investment tax credits taken in excess if the unit is withdrawn from the integrated rental program before the end of the ten (10) year period, or b) one of the two parties shall pay, at the time of the purchase and sale, any tourism investment tax credit taken in excess computed as if the unit had been withdrawn from the integrated rental program on the date of the purchase and sale of the unit.

§5(d)-8. Examples. (i) Investor A purchases on January 1, 20X0, a unit in a Condohotel, complying with all of the requirements of the Act, for the total price of \$200,000, of which he pays \$40,000 in cash. On February 1, 20X0, he dedicates the unit to the integrated rental program ("the program"). For tax year 20X0, A takes with his income tax returns, filed on April 15, 20X1, a tourism investment tax credit equal to \$10,000 (which is half of the total credit of \$20,000 to which he is entitled). On June 1, 20X1, he withdraws the unit from the program. Investor A will owe as income taxes the amount of \$8,000 (\$10,000 of tourism investment tax credit taken less \$2,000, which is the result of the mathematical operation in which the \$20,000 [the total tourism investment tax credit to which he would have been entitled had

he kept the unit in the program for ten years] is multiplied by $1/10$, (the fraction in which the numerator is the number of years in which the unit was in the program [1 year] and the denominator is ten). The tax debt must be paid in two parts, \$4,000 with the tax return for the year 20X1, and \$4,000 with the tax return for the year 20X2.

(ii) Under the same fact pattern of the preceding example, if A takes a tourism investment tax credit of \$10,000 in the year 20X0, and another tourism investment tax credit of \$10,000 in the year 20X1 (to complete the total \$20,000 to which he is entitled) and he decides to withdraw his unit from the integrated rental program on February 1, 20X8, the computation to determine the amount owed would be the following:

Total credit taken	\$20,000
Minus (-) total credit to which he was entitled (\$20,000) multiplied by $8/10$	\$16,000
Amount owed	\$ 4,000

§5(e)-1. Loss in the Disposition of an Eligible Investment or Participation in a Fund. Subject to the conditions provided herein, any loss suffered in the sale, exchange or other disposition, including redemption or liquidation, of an Eligible Investment or participation in a Fund in a *bona fide* transaction by an Investor or Participant who is not a Developer, even when the Tax Exemption Concession has expired for any reason, shall be considered a capital loss, but an

Investor or Participant who is not a Developer, will have the option of taking such loss as a credit against his tax liability in the tax year of said loss and in the following four (4) tax years. In order to determine the amount, if any, of a loss for purposes of the credit for loss of Article 5(e) of the Act, particular attention shall be paid to the nature of the transaction, to the terms of the contract in which the credit is disposed of and the existence of other relevant circumstances, such as, for example, the existence of a repurchase agreement. The amount of the loss which may be taken as credit in each of the years indicated above may not exceed one third (1/3) of the amount of the loss.

For purposes of determining the amount of the loss credit, the basis of the participation in a special partnership shall not be adjusted to reflect the increases to said basis calculated according to Supplement P of the Income Tax Act. On the other hand, any reduction in the basis determined according to Supplement P shall be recognized for purposes of the computation of the loss credit, but only up to the amount of the tax benefit derived by the Investor or Participant in the transaction or event which gave rise to the reduction in the basis under Supplement P.

The total amount of the Eligible Investment or participation in a Fund which may qualify for the loss credit may not exceed 20% of the total cost of the Tourism Project. In cases in which the Eligible Investments or participations in a Fund

exceed 20% of the total cost of the project, the Investors and Participants shall distribute the right to benefit from the credit using the mechanism provided in Article 5(c) of this Regulation. The loss credits may not be assigned or transferred, for which reason the provisions of Article 5(f) of the Act referring to assignment, sale or transfer of the credit shall not apply.

Any excess of the credit so granted over the Investor/Participant's tax liability during the aforementioned five (5) tax years may not be taken as a deduction or a credit, nor carried back or carried over to another tax year.

§5(e)-2. Examples. (i) Taxpayer A purchases 100 shares of Exempt Business X, a corporation, for \$10,000 in the year 20X0. The entire \$10,000 invested by A qualifies as Eligible Investment, for which the latter takes a tourism investment tax credit of \$2,500 in the year 20X0 and a tourism investment tax credit of \$2,500 in the year 20X1, for a total of \$5,000, which represents 50% of his Eligible Investment of \$10,000. As a result of the tourism investment tax credit taken, A's basis in his shares in Corporation X are reduced from \$10,000 to \$5,000. Corporation X generates losses during the years 20X0 and 20X4. The portion of said losses attributable to A is \$2,000 during each of these five (5) years for a total loss of \$10,000, but A will not obtain any tax benefit from such losses since under the provisions of the Income Tax Act of 1954, the losses of the corporation do not pass on directly to

its shareholders. Therefore, A's basis in its 100 shares of Corporation X shall remain at \$5,000. Corporation X files for bankruptcy during the year 20X5 and the shares of said company lose all of their value. Regardless of whether Taxpayer A's loss occurred before or after the date of expiration of Corporation X's Tax Exemption Concession, Taxpayer A shall be entitled to take a \$5,000 deduction against his income for the year 20X5, and will also have the option of taking a \$5,000 credit against its tax liability, as long as the amount taken in a specific year does not exceed 1/3 part of \$5,000 (\$1,666-.66). The total credit must be taken prior to the year 20X9, that is, within four (4) years following the occurrence of the loss.

(ii) Continuing with the same fact pattern of example (i), if Exempt Business X were a Special Partnership under Supplement P of the Income Tax Act, and Taxpayer A paid \$10,000 for a 2% interest in said partnership, A could, under the rules of Supplement P, take a deduction of \$2,000 against his income during the years 20X0 through 20X4. Assuming that A's income during each of those five (5) years was such that he had to file returns on the basis of a 30% tax rate, the tax benefit generated by that \$2,000 deduction per year during the years 20X0 through 20X4 would be \$3,000 (\$600 per year for five (5) years). A's basis for his interest in Special Partnership X in the year 20X5 would be \$2,000 (the \$10,000 he originally paid, less the \$5,000 taken as tourism

investment tax credit, less the tax benefit of \$3,000 generated by the business' losses). In the year 20X5, when A's participation in the Special Partnership loses all of its value, A may take a deduction of \$2,000 against his income, and will also have the option of taking a credit of \$2,000 against his tax obligation. The amount of credit taken in a specific year may not exceed \$666.00 (1/3 of \$2,000), and the total credit must be taken before the year 20X9.

(iii) Taxpayer A buys 100 shares of Exempt Business Y, a corporation, for \$10,000 in the year 20X0. The entire \$10,000 invested by A qualifies as an Eligible Investment, so A takes a tourism investment tax credit of \$2,500 in the year 20X0 and a tourism investment tax credit of \$2,500 in the year 20X1, for a total of \$5,000, which represents 50% of his Eligible Investment of \$10,000. As a result of the tourism investment tax credit taken, A's basis in his shares in Corporation Y are reduced from \$10,000 to \$5,000. Corporation Y generates income immediately and during the years 20X0 through 20X3, the portion of such income attributable to Taxpayer A is \$2,000 per year. However, Corporation Y does not distribute dividends to any of its shareholders. According to the applicable provisions of the Income Tax Act, Taxpayer A's basis remains at \$5,000. Likewise, for purposes of determining the loss credit available under Article 5(e) of the Act, A's basis also remains at \$5,000. Therefore, if Taxpayer A decides to sell his shares

of Corporation Y in the year 20X5, he shall not be entitled to any loss credit unless he sells the shares for less than \$5,000.

(iv) The same fact pattern as example (iii), but assuming that Exempt Business Y is a Special Partnership under Supplement P of the Income Tax Act. Taxpayer A pays \$10,000 for a 2% interest in said partnership; the total \$10,000 invested by A qualifies as an Eligible Investment, for which A takes a tourism investment tax credit of \$2,500 in the year 20X0 and a tourism investment tax credit of \$2,500 in the year 20X1, for a total of \$5,000, which represents 50% of its Eligible Investment of \$10,000. As a result of the tourism investment tax credit taken, Taxpayer A's basis in Special Partnership Y is reduced from \$10,000 to \$5,000. Special Partnership Y generates income immediately. During the years 20X0 through 20X3, the annual portion attributable to Taxpayer A of said income is \$2,000. However, Special Partnership Y does not make any distribution to any of its partners. According to the provisions of Supplement P of the Income Tax Act of 1954, Taxpayer A must recognize as income the portion of the income from Special Partnership Y attributable to his partnership interest, and the basis of such interest shall increase in the same amount as the income recognized even if it has not been distributed. Therefore, for purposes of Supplement P, the basis of Taxpayer A's participation in Special Partnership Y shall increase by

\$8,000, for a total of \$13,000; however, for purposes of determining the amount of loss credit available under Article 5(e) of the Act, the increase of \$8,000 shall not be considered and Taxpayer A's basis shall remain at \$5,000. Taxpayer A shall not be entitled to any loss credit unless he sells his participation in Special Partnership Y for less than \$5,000.

§5(f)-1. Tourism Investment Tax Credit; Sale, Assignment or Transfer; Requirements; Reports. A tourism investment tax credit may be transferred, sold or otherwise assigned after the Exempt Business has notified the distribution of the tourism investment tax credit among its Investors and Participants. A tourism investment tax credit may only be transferred, sold or otherwise assigned by the Person who is an Investor or Participant.

The transfer, sale or other assignment of a tourism investment tax credit by an Investor or Participant must be made through a sworn statement which shall include the information provided for in §5(f)-4 of this Regulation. A certified copy of said sworn statement shall accompany the income tax return for each year in which the transferee wishes to take all or part of the tourism investment tax credit assigned to it. He who acquires a tourism investment tax credit from an Investor or Participant through transfer, sale or other form of assignment, does not become an Investor or Participant; however, the credit assigned shall maintain its original characteristics for purposes of the limitation of

Article 5(a) of the Act and its corresponding sections in this Regulation to the effect that no more than half of the credit generated by an Eligible Investment may be taken during the credit's first tax year of availability. The Developer of a Tourism Project may neither assign nor be the assignee of the tourism investment tax credits originating from said Tourism Project.

§5(f)-2. Sale or Assignment of Tourism Investment Tax Credits.

Adjustment of the Basis of the Eligible Investment. The amount of tourism investment tax credit assigned shall reduce the adjusted basis of the assignor's Eligible Investment in an amount equal to the tourism investment tax credit.

§5(f)-3. Sale or Assignment of Tourism Investment Tax Credits; Amount which shall be Tax Exempt. Any property or money received in exchange for a tourism investment tax credit assigned shall be tax exempt up to an amount which is equal to the amount of the tourism investment tax credit assigned. The amount paid for a tourism investment tax credit may not be taken as a deduction, nor may it be capitalized or otherwise considered to be an expense under the Income Tax Act. Likewise, when the amount paid for a tourism investment tax credit by the buyer/assignee is less than the amount of the credit, the difference shall not be considered income by the buyer/assignee nor a loss by the seller/assignor of the credit.

§5(f)-4. Sale or Assignment of Tourism Investment Tax Credits. Notices. The assignor and the assignee of a tourism investment tax credit shall notify the Director and the Secretary of the assignment through a sworn statement therefor which shall include: (i) the name, address and social security number of the assignor, (ii) the name, address and social security number of the assignee, (iii) the total amount of the tourism investment tax credit approved by the Director, (iv) the total amount of the tourism investment tax credit of the assignor, (v) the amount of tourism investment tax credit taken by the assignor, (vi) the amount of tourism investment tax credit assigned, (vii) the date of the assignment and the tax year in which the tourism investment tax credit assigned may be taken according to the provisions of Article 5(a) of the Act and the corresponding sections of this Regulation, (viii) the consideration given in exchange for the tourism investment tax credit, and (ix) a statement to the effect that the assignor is not the Developer of the Tourism Project for which the tourism investment tax credit was granted. Said notice shall be included with the income tax returns of the assignor and the assignee for the year of the assignment.

§5(f)-5. Credits Assigned by the Government of Puerto Rico. When the assignor of the tourism investment tax credit is the Commonwealth of Puerto Rico through any of its agencies, instrumentalities or public corporations, pursuant to the provisions of §5(f)-4 of this Regulation, it shall be neces-

sary to obtain the express approval for the assignment of the credit from the Director, the Secretary and the President of the Government Development Bank of Puerto Rico.

\$5(f)-6. Examples. (i) Taxpayer A and Taxpayer B make Eligible Investments through the purchase of participations in a Fund for a total of \$100,000 each on January 1, 20X0. The adjusted basis of each shall be \$100,000. In 20X0, each takes the amount of \$25,000 as tourism investment tax credit, reducing their adjusted basis in the Eligible Investment to \$75,000. On February 15, 20X1, Taxpayer B sells to Taxpayer A the remainder of its tourism investment tax credit of \$25,000, for \$20,000. Taxpayer B reduces its adjusted base in its Eligible Investment by \$25,000, to \$50,000. Taxpayer A may take \$50,000 of tourism investment tax credit in 20X1; \$25,000 for its Eligible Investment and \$25,000 for the tourism investment tax credit acquired from Taxpayer B. After taking the entire credit, the adjusted base of Taxpayer A in its Eligible Investment shall be \$50,000. The \$20,000 received by Taxpayer B from the sale of its tourism investment tax credit are tax exempt. Taxpayer A may not take a deduction for the \$20,000 which it paid for the tourism investment tax credit, nor may it capitalize them or consider them as an expense under the Income Tax Act, but the \$5,000 difference between the tourism investment tax credit received (\$25,000) and the purchase price (\$20,000) shall not be considered to be income for purposes of the Income Tax Act of 1954.

(ii) Investor A makes an Eligible Investment prior to filing his income tax return for the year 2000 which generates a tourism investment tax credit of \$1,000. According to the provisions of Article 5(a) of the Act and the corresponding sections of this Regulation, Investor A shall be entitled to take a \$500 tourism investment tax credit in tax year 2000 as a result of said Eligible Investment. A sells to his friend B \$800 in tourism investment tax credits, but he wishes to take the remaining \$200 of tourism investment tax credits with his income tax return for the year 2000. The sworn statement which he must execute pursuant to the provisions of §5(f)-1 in order to make the purchase and sale must contain a statement specifying that of the \$800 which are being sold, B may only take \$300 with his income tax return for the year 2000.

§5(g)-1. Special Rules for Investments Made by Investment Capital Funds created Under Act No. 3 of October 6, 1987, as Amended. An Investment Capital Fund created under Act No. 3 of October 6, 1987, as amended ("Act No. 3") which makes an Eligible Investment in an Exempt Business shall be entitled to the tourism investment tax credit provided by the Act, but the credit shall be limited to the 25% provided by Article 5(g), contrary to the 50% provided by Article 5(a) of the Act. This limitation is based on the fact that the investors in a Fund created under Act No. 3 already enjoy a tourism investment tax credit of 25%, pursuant to the provisions of said act.

Insofar as the tourism investment tax credit under the Act for Investors who invest in an Exempt Business may not exceed 50% of their cash investment, it is not possible to offer the Funds under Act No. 3 a tourism investment tax credit greater than 25%. The loss credit provided by Article 5(e) of the Act shall not be available to Funds under Act No. 3.

§5(g)-2. Example. The total cost of the project of Exempt Business Z is \$50 million. The Developer of the Exempt Business invests \$10 million in cash and an Investment Capital Fund organized under Act No. 3 invests \$5 million. The maximum amount of tourism investment tax credit which may be taken by the Investors/Participants of Exempt Business Z shall be the lesser of: (a) 10% of the total cost of the tourism project (\$5 million), or (b) 50% of the cash contributed by the Investors/Participants (\$7.5 million). Since the maximum amount of tourism investment tax credit available to the Fund under Act No. 3 is 25% of its cash investment, the credit available to the Fund shall be \$1.25 million. For purposes of computing the entire tourism investment tax credit available for the Tourism Project, however, it shall be understood that the Fund organized under Act No. 3 took 50% of its investment in cash, that is \$2.5 million. Therefore, the maximum amount of credit which the Developer may take shall be \$2.5 million.

§6(a)-1. Renegotiation of a Tax Exemption Grant; Distribution of Accrued Profits; Carryover of Losses. Any Exempt Business

which enjoys tax exemption under any of the Industrial Exemption Acts or the Tourism Incentives Act of 1983 may apply for a Concession under the Act as long as it complies with all of the requirements thereof and of this Regulation, including the requirements of "substantial renovation or expansion" specified in §2(g)-2 hereof, and surrenders its tax exemption grant under the aforementioned acts.

§6(b)-1. Renegotiation of a Tax Exemption Grant Issued under the Industrial Incentives Acts or the Tourism Incentives Act of 1983. Any Exempt Business which adopts the benefits of Article 6 of the Act, and receives a Concession thereunder, shall enjoy the benefits of the Act for the period set forth therein.

§6(c)-1. Accrued Profits Prior to the Date of the Renegotiation. Profits accrued prior to the date of the renegotiation shall be distributed under the terms of the tax exemption grant under which these profits were obtained.

§6(d)-1. Cases of Renegotiation; Tax Rules. An Exempt Business which receives the benefits of the Act through Article 6 thereof, shall be taxed at the time of its liquidation, as follows:

(i) on Tourism Development Income (which by definition are those generated under the Act), pursuant to the provisions of the Act;

(ii) on the income accrued prior to the date of commencement of their Tourism Activity, pursu-

ant to the provisions of its prior tax exemption grant.

§6(e)-1. Cases of Renegotiation; Carryover of Losses. The net losses which the Exempt Business is carrying over shall be divided into exempt and non-exempt in order to be taken in accordance with the provisions of Article 3(c)(1)(G) of the Act and its corresponding sections hereof. Net losses being carried over that were generated under the previous tax exemption grant in a year in which an election similar to that of Article 3(a)(1)(D) of the Act was in effect, may only be used against profits generated in a year in which the election under Article 3(a)(1)(D) is in effect.

§7(a)-1. Transfer of a Concession; Approval by the Director; Consequences. A Concession may not be transferred without the prior authorization of the Director. Neither can there be a transfer of stock, participations, property or any majority interest in an Exempt Business, even when the Business continues to be dedicated to the Exempt Activity or the property to the same Tourism Activity, without the prior written authorization of the Director. Any transfer of this kind will annul the Concession at the moment of its transfer.

§7(a)-2. Retroactivity. Any transfer made without the prior approval of the Director may be approved retroactively, when the Director is of the opinion that it is in the best interests of Puerto Rico under those particular circumstances.

§7(a)-3. Filing of an Application. For purposes of applying for approval of a transfer pursuant to Article 7(a) of the Act, the applicant shall comply with the requirements of Article 9(c) of the Act. For purposes of an application for a transfer, the term within which the Director shall issue a final ruling in writing, as well as the rest of the terms granted by Article 9(c), shall be sixty (60) days.

§7(b)-1. Transfers which Do Not Require Prior Approval. The following transfers do not require the prior approval of the Director, except when otherwise indicated:

- (i) the transfer of the assets of a decedent to his estate or the transfer by legacy or inheritance;
- (ii) the transfer of the stock or an interest in the Exempt Business when said transfer does not result directly or indirectly in a change in the dominion or control of the Exempt Business;
- (iii) the pledge or mortgage executed during the ordinary course of business for the purpose of providing a guarantee of a *bona fide* debt. Any transfer of control, title or interest by virtue of said contract shall be subject to the provisions of subparagraph (a) of Article 7 of the Act;
- (iv) the transfer by operation of law, by order of a court or a bankruptcy judge to a fiduciary trustee. Any subsequent transfer to a third party who is not the same debtor shall be subject to the

provisions of subparagraph (a) of Article 7 of the Act.

§7(c)-1. Transfers which Do Not Require Prior Approval; Notice. Any transfer which does not require the prior approval of the Director shall be reported by the Exempt Business to the Director within thirty (30) days of its occurrence. Such transfer shall be notified by certified mail and shall include all of the information required by Article 9(c) in an application for a Concession.

§8(b)(3)-1. Condohotels. Fines and Annulments due to Breaches of the Conditions of their Concession. Any Investor who is the owner of a unit in a Condohotel and wishes to reserve the same to use it for more than thirty (30) days per year, or to use it as a "walk-in" for more than the sixty (60) days per year provided for in this Regulation shall pay, for each day in excess, the prevailing daily rate and related charges applicable to travelling guests at the time the Investor uses the unit. The operator of the Condohotel shall be responsible for collecting said rate. The Director shall impose a fine equal to triple the aforementioned daily rate, multiplied for each day in which the unit is used in excess of the number of days permitted herein without paying the prevailing daily rate, to any operator who permits an Investor to reserve and use his unit for more than thirty (30) days or to use it as a "walk-in" for more than sixty (60) days without

complying with the provisions hereof. The Concessions of the operators and Investors who incur in three or more violations of this section may be revoked by the Director at his discretion. Likewise, the Concessions of operators who alter their books to avoid the application of this section shall be summarily revoked.

§8(b)(3)-2. Puerto Rican Paradors; Separation from the Parador Program; Renegotiation of their Concession. Any Puerto Rican Parador which voluntarily resigns or is separated by the Puerto Rico Tourism Company from the parador program which it sponsors may renegotiate its Concession under the Act, if it complies with the provisions of Article 6 thereof and any other applicable provision.

§9(a)-1. Administration of the Act; Administrative Rulings. The Director may from time to time issue administrative rulings and circular letters regarding the application of any specific provision of the Act or of this Regulation.

§9(c)-1. Applications; Terms; Requirements; Administrative Procedure. Applications for a Concession under the Act. Anyone applying for a Concession under the Act shall submit together with his application the following documents, in full force, as applicable:

1. A sworn statement which contains the following information, in detail;

- a. Name, address and social security number of the Person who is applying for the Concession.
- b. Name and address of the legal representative.
- c. Nature of the Eligible Business.
- d. Name of the Investors and their social security numbers.
- e. Legal provision under which the Concession is requested and explanation of why the Business qualifies therefor.

2. If it is a domestic corporation, a copy of the certificate of incorporation issued by the Department of State; if it is a civil partnership, a copy of the Partnership Agreement; if it is a Business partnership, a certificate from the Registrar of Property to the effect that it is recorded in the Mercantile Registry; if it is a foreign corporation, a certificate issued by the Department of State authorizing it to do business in Puerto Rico; if it is a special partnership, a copy of the election submitted to the Secretary; in the case of other juridical persons, faithful evidence thereof.

3. The audited financial statements of the last two tax years in cases of Existing Businesses or, in cases of New Businesses, the unaudited financial statements of the principal stockholders or partners. For

purposes of this subparagraph, a "principal stockholder or partner" shall be considered to be anyone who by himself or in conjunction with another who is affiliated with, owned by or directly or indirectly controlled by said stockholder or partner owns ten percent (10%) or more of the shares or interests in the Eligible Business. The shareholders in Tourism Investment Capital Funds shall be exempt from the provisions of this subparagraph.

4. An inventory of any real or personal property which will be used or is used in the Eligible Business.

5. A negative certificate of debt from the (i) Collections Bureau of the Department of the Treasury, (ii) Excise Tax Bureau, (iii) Center for Municipal Income Collection, (iv) Department of Labor, and (v) State Insurance Fund to the effect that the petitioner does not owe any taxes, assessments, excise taxes or fees of any kind. If the petitioner is a New Business or has never filed income tax returns nor paid fees in any of the areas covered in this subparagraph (v), the corresponding negative debt certificate shall identify the business as a New Business or explain the reasons why the corresponding fees have not been paid.

6. Use, construction or location permit, according to the stage of development which the Eligible Business is in.

7. Alcoholic Beverages License.

8. Certificate of Public Establishment issued by the Department of Health.

9. Municipal License.

10. Certificate of Inspection by the Puerto Rico Fire Service.

11. The blueprints of the project and an itemization of the facilities.

12. Certificate of public liability insurance issued by an agency certified by the Office of the Commissioner of Insurance of Puerto Rico.

13. Number of direct permanent full time jobs which the business generates or will generate and the term within which they will be generated.

14. Number of part-time jobs which the business generates and/or will generate and term within which they will be generated.

15. Amount of the payroll.

16. Investment made and/or to be made (description and amount), including:

a. budgets prepared for purposes of feasibility studies or for construction proposals

b. estimate of the tourism investment tax credit which will be available for the Investors and Participants and a proposal of the manner in which the credits will be distributed.

17. Location or site of the Tourism Activity.
18. Identification and description of the facilities for persons with physical disabilities.
19. Safety measures for the benefit of the clients.
20. Improvements and maintenance plan for the physical facilities and for the environmental and aesthetic infrastructure.
21. Promotion, publicity and marketing plan.
22. Training and retraining plan for personnel.
23. Proportion of the net income which the petitioner proposes to invest in subparagraphs (18), (19), (20), (21) and (22). If the operation of the business is to be shared by the owner and the operator thereof, the proportion of the net income invested by each of them and by both of them collectively shall be taken into consideration.
24. Estimated date of commencement of the Tourism Activity.
25. Receipt evidencing that the application was filed with the Department of the Treasury.
26. Any other document or information which the petitioner deems convenient to submit or which the Company deems necessary in order to undertake a full and complete examination of the Petitioner's application.

Should the petitioner believe that one or more of the complementary documents enumerated herein do not

need to be presented at the time of the filing of the application, he shall accompany a sworn statement stating the reasons for such decision and stating that the documents shall be submitted subsequently. The Tax Exemption Concession shall be conditioned upon the submission of the applicable documents which were originally omitted prior to the time in which the Exempt Business opens its doors to the public, in the case of a New Business, or completes its substantial renovation or expansion, in the case of an Existing Business. In these cases, the procedure established in the regulation governing the Tourism Company's Uniform Administrative Procedure shall be followed with respect to §9(c)-2 hereof.

§9(c)-1(a). Condohotels. In the case of Condohotels, the Developer shall file an application for a master Concession for the project which shall meet all the requirements of the Act and of this Regulation. Said application shall also identify the horizontal property regimes which are included in the program, and all of the units which will comprise said program and it shall include the master deed of said horizontal property regime, as well as the by-laws of the owners' association. The application must also include a sworn statement that provides (i) the date on which the construction of the Condohotel was (or shall be) finished; (ii) that the units of the Condohotel have never been used (or will never be

used) for any other purpose, and (iii) that the units were (or shall be) acquired directly from the person or juridical entity who constructed or developed the Condohotel.

The individual Investors who acquire each unit shall comply with the requirements of this section through the filing of an application for a supplementary Concession. Said application shall not contain the information provided for in §9(c)-1 of this Regulation. Instead, it shall state the case number of the master Concession, identify the particular unit, and include the documents mentioned in Article 9(c) of the Act, the unaudited financial statements of the Investor or any other document acceptable to the Director which contains information regarding his financial capacity, the management agreement with the operator of the integrated rental program, the deed of purchase and sale, the deed(s) of any mortgage(s) which may encumber the unit, and a sworn statement from the seller of the unit to the effect that the difference between the sale price and the sum of the mortgage(s) which encumber the unit was paid in cash. The Director shall notify the individual Investor directly of his decision regarding the Concession based on the documents presented to him.

§9(c)-2. Filing of the Application. In order to process an application for a Concession under the Act, the petitioner must file, by mail or in person, the original and three (3) copies of the application, directed to the attention of the Director, accompanied by the complementary documents. At the

time of filing his application with the Director, the petitioner must file a certificate or receipt proving that he filed a copy of the application and of all of the complementary documents with the Secretary. The fee for processing tax exemption applications under the Act at the Department of the Treasury shall be determined by said Department.

The application filed with the Tourism Company must be accompanied by a certified check or bank draft or money order from the U.S. Postal Service payable to the "Executive Director of the Tourism Company" in the amount which from time to time will be determined by the Director through circular letter therefor. Until the first of said circular letters is issued, the fee for processing tax exemption applications shall be \$500.00, and \$100.00 in the specific case of paradors and hostelries of fifteen (15) rooms or less. The employee to whom the application is assigned shall fill out the corresponding checklist and shall issue a copy thereof to the petitioner. The checklist shall indicate the date and time of receipt of the application and the signature of the official. In the event that the application is incomplete, the Tourism Company official will so indicate it in the checklist, and the application shall be considered to be have been filed provisionally. In such cases, the terms set forth in §9(c)-3 hereof shall not begin to run until the petitioner files the original and three (3) copies of the required documents. Once said documents have been filed, the official shall sign the

checklist and shall place the date and time of receipt of the application duly filed.

§9(c)-3. Term. The Secretary shall submit his recommendation to the Director no later than sixty (60) calendar days after receipt of the duly filed application. If the recommendation is not received within the aforementioned sixty (60)-day period, it shall be understood that the same has received a favorable recommendation from the Secretary. The Company shall examine the application, inspect the petitioner's business when it determines that it is necessary to do so, and the Director shall make the corresponding decision within one hundred and twenty (120) days from the date the application was duly filed.

The Company need not conduct the aforementioned inspection when the petitioner's facilities have not been constructed, are not in operation, or when the documents submitted show that it does not meet the requirements of the Act or of this Regulation, or for any other justified circumstance.

§9(c)-4. Criteria to be Used by the Director. The Director shall determine the eligibility of the petitioner taking into account the nature of the physical facilities; the number of employments generated by the owners, operators and/or administrators of the Exempt Business, and any other factors which he believes are pertinent for such a determination, considering the best economic and social interests of the People of Puerto Rico.

Having made the corresponding decision with respect to the application, the Director shall proceed as follows in the case of:

A. Acceptance

He shall notify his decision by mail through a written communication to the petitioner and to the Secretary. The Concession may be conditioned upon the petitioner's compliance with certain requirements or conditions. The Concession shall itemize all of the conditions under which it is issued, including:

1. The percentage of exemption for each of the exemptions granted under Article 3 of the Act.
2. The deadline for commencement of the Tourism Activity.
3. The total cost of the Tourism Project and the items which may be considered as part of the cost of the Tourism Project.
4. A certificate of eligibility for investment by a Fund.
5. The preliminary maximum amount of tourism investment tax credit available for the Tourism Project.

B. Denial

He shall notify the denial in writing by certified mail, with a copy to the Secretary, stating the reasons upon which he bases his denial.

Having notified the denial by virtue of the provisions of this subparagraph, the petitioner may:

1. Request from the Director a discretionary term not greater than ninety (90) working days, computed as of the date on which the petitioner receives said notice of denial, to rectify or correct the deficiencies pointed out. Said ninety (90) day term may be extended by the Director, motu proprio or at the request of the petitioner, when the deficiencies pointed out are such that their correction requires a greater period of time. The petitioner may request a re-evaluation of his case once the deficiencies have been corrected and if it is determined that he complies with the requirements, then the procedure shall continue pursuant to §9(c)-3 hereof.

2. Request that within thirty (30) days from the receipt of said notice of denial, the Director reconsider his decision pursuant to the procedures set forth in Article IX of the Uniform Administrative Procedures Regulation of the Tourism Company. Having satisfied these procedural guarantees, the Director's ruling shall be final.

§9(c)-5. Inspections of the Facilities of the Exempt Business. Once the inspections mentioned in §9(c)-3 have been conducted, if necessary, and the Concession requested has been approved, the Tourism Company shall conduct any further inspections it deems necessary to determine faithful compli-

ance with the provisions of the Act and of this Regulation or with the conditions imposed in the Concession issued pursuant to §9(c)-4, subparagraph (A) hereof, if any, including verification that the various applicable governmental certificates are updated. The officials of the Tourism Company shall have free access to the business during working hours to conduct such inspections.

§9(d)-1. Promotional Plan.

A. The promotional, publicity and marketing plan required in §9(c)-1 shall contain the following:

1. Identification of the business' target market.
2. Goals and objectives directed to that market.
3. Strategies and programs to reach said goals and objectives.
4. Identification of any cooperative promotional plans with other components of the industry.
Said plans shall contain, in addition to the business' own attractions, those natural or historical attractions offered by the Island.
5. Economic feasibility study of the project.

B. The Exempt Businesses, in coordination with the Tourism Company, shall supply information and/or promotional material to their guests or the users of their facilities regarding the activities, excursions, places for entertainment and/or of tourism interest in Puerto Rico, as well as the official tourism guide of the Tourism Company.

§9(d)-2. Safety Measures.

A. Among the elements to be considered as part of the safety measures which the Exempt Business must maintain are the following:

1. Obtaining and maintaining the Certificate from the Puerto Rico Fire Service according to and as required by the periodic inspections undertaken by the Fire Service.

2. Training its employees in the identification and course of action to be followed when any activity, person or object represents a threat to the safety of the clients or the establishment.

3. Maintaining a public liability insurance policy according to and as required by the Tourism Company which shall include said Company as an insured.

4. One or more first aid kits duly equipped, depending upon the number of clients and employees.

5. A list of hospitals, doctors and pharmacies which may be easily contacted in case of an emergency.

6. Obtaining and maintaining the corresponding permits from the Department of Health, the Regulations and Permits Administration and the Department of Sports and Recreation necessary for the operation and/or use of the swimming pools and public beaches.

7. Providing the proper maintenance and vigilance and complying with the relevant provisions of law with

respect to beaches, lakes or rivers bordering its facilities.

8. Placing an emergency exit floor plan in the hallways of each floor.

9. Measures in addition to those required by the Fire Service to prevent or reduce the spread of a fire in rooms with and without kitchens.

10. Equipment which guarantees the safety of the guests in their rooms, such as for example, locks, peepholes and/or internal latches on the entrance and exit doors of the rooms, as well as on the connecting door between two or more rooms.

11. Identification of all of the rooms on their entrance doors.

§9(d)-3. Cleaning; Lighting; Arrangements and Comfort Measures for the Clients and/or Guests of the Exempt Business.

A. Exempt Businesses shall maintain the public spaces, rooms (when applicable), and other facilities, clean and attractive and with furnishings, accessories and equipment which is comfortable and of good quality and appearance. They shall likewise comply with the following requirements:

1. Maintain all signs, entryways, gardens, parking lots and outdoor and interior areas of public use, attractive, clean and adequately lit.

2. There shall be a specific area for solid waste, with waste cans or bins with covers made of a resistant

material. The same shall be located in such a way that they will not affect the aesthetics of the establishment and they shall be easy to clean and to maintain in good condition.

3. Air conditioners, water heaters and other equipment shall be installed in accordance to the applicable Safety Code of the Electric Power Authority. Such installations and equipment shall be in perfect working condition and shall be periodically revised by competent personnel.

4. Wastewaters shall be eliminated through the public sewer network, or should the latter not exist, through an efficient system adjusted to the sanitary standards in effect.

5. There shall be rest rooms for both sexes in the areas of common use, according to the number of clients and employees. The rest rooms shall have toilets, washbasins and, in the men's room, urinals.

6. All of the areas and installations shall be in perfect hygienic conditions. In this regard, the Exempt Businesses shall have the approval of the Puerto Rico Department of Health and of the Tourism Company.

7. There shall be full compliance with the applicable safety and health regulations.

8. The bar, if there is one, shall be kept visually or physically separated from the dining area,

thus maintaining the elements of good taste and hygiene required in all facilities.

B. Exempt Businesses which have kitchen facilities shall comply with the following requirements, in addition to those required by subparagraph A hereof:

1. The walls, ceilings and floors of the kitchen shall be of waterproof material with no breakage or rough places, so as to facilitate their cleaning. Anti-skid and waterproof materials shall be used for the floors, and material which does not accumulate dirt or grease shall be used for the walls, tiles and smooth surfaces.

2. Depending on the type of business, the kitchen shall be provided with the necessary equipment, such as, for example: oven, stove, refrigerator with a separate area for meats and fish, a refrigerator to store milk-based products, a freezer and table to defrost foods, in addition to fire extinguishers, extractors and trash cans with bags. It shall also have adequate ventilation and lighting.

3. The refrigerators and freezers shall be in good working condition. The oven grills must be made out of rustproof materials.

4. They shall have dishwashers for cleaning silverware. Alternatively, they shall use a process of equal sanitary condition using hot water and detergents which ensure that the utensils will be germ-free.

5. The kitchen's pantries must contain shelves and elevated cabinets, placed at least one foot (1') over the level of the floor. There shall also be a place or places inaccessible to pests and animals to store foodstuffs which are not packaged.

C. Hostelries shall comply with the following requirements, in addition to those required in subparagraphs A and B hereof:

1. A reception area which includes, among others: a registration, information and cashier desk; mail and message handling; men's and women's separate rest rooms, and a safe, if a safe is not conveniently provided elsewhere.

2. Parking space, pursuant to the regulation promulgated by the Planning Board, as amended, applicable to hostelries located in urban zones. Hostelries located in rural zones shall provide one (1) parking space for every two (2) rooms plus one (1) parking space for every dining room or restaurant table, unless there are adequate parking facilities close to the hostelry.

3. Loading and unloading zone.

4. Administrative Offices which, depending upon the size of the hostelry, shall have a place to store luggage.

5. Dining room or restaurant whose size and number of tables is proportional to the number of rooms and minimum services to be offered to guests and users.

6. Kitchen area, which shall comply with the requirements of the Department of Health, and a service and storage area.

7. All of the bedrooms in the hostelry shall have, at least, the following equipment, furnishings and fixtures:

- a. One bed, single or double, or two single beds.
- b. One or two night tables, separated from or attached to the headboard.
- c. One armchair, easy-chair or chair and a small table or desk.
- d. One chest of drawers, or a shelf unit.
- e. One closet with sufficient hangers.
- f. One luggage rack.
- g. One or two area rugs, depending on the number of occupants, placed close to the bed(s), unless the floor of the room is completely carpeted.
- h. Adequate general lighting and reading lamps which can be operated from the beds.

- i. One window, glass door or other aperture which allows visibility from the room and which is covered with blinds or curtains so as to obstruct the passage of light when the guest so desires, and screens, when required by the Tourism Company.

8. The size of the bedrooms shall be in proportion to the number of occupants.

9. All bedrooms shall have adequate natural or artificial ventilation.

10. Bedrooms with their own, individual bathrooms. The bathrooms will have adequate ventilation and will be provided with, at least, the following equipment, furnishings and fixtures:

- a. Shower with curtain
- b. Wash basin
- c. Toilet
- d. Hot and cold running water at all times
- e. Light and a mirror
- f. Shelf for toiletries
- g. Safety handrail in the tub or shower
- h. Bath rug
- i. Bath soap
- j. Toilet paper
- k. Waste basket

Guest Houses shall have one bathroom per bedroom.

11. The bedrooms shall not have direct access to the street in facilities which have a family home environment.

12. All bedrooms with kitchen facilities shall also comply with the requirements contained in subparagraph B hereof.

§9(d)-4. Accessibility for the Disabled. Exempt Businesses shall provide facilities for the disabled, such as access ways, elevators, parking, sanitary services and appropriate light switches and shall comply with the provisions of the applicable local and federal laws. If they do not have these facilities at the time of application for the Concession, steps must be taken to comply therewith within a period not greater than twelve (12) months from the date the Concession is approved, except when otherwise provided by law.

§9(d)-5. Additional Comfort Measures for the Clients and/or Guests.

A. Exempt Businesses shall offer the following services:

1. Businesses whose facilities border on beaches, lakes, lagoons or rivers, shall maintain a program for cleaning the same and shall coordinate with the corresponding governmental agency in this regard.

2. Public telephones within their premises. Hostelries shall also provide a private telephone in each

bedroom or, instead, a public telephone in the common areas.

3. They shall inform the Tourism Company of any service which they offer or will offer to their clients.

B. Hostelries shall offer the following services, in addition to those required in subparagraph A hereof:

1. They shall receive, safeguard and deliver their guests' their luggage, correspondence and messages and shall comply, as far as possible, with their requests.

2. The bedrooms shall be clean and ready at the time of the guests' arrival.

3. There shall be special personnel in charge of cleaning and the daily preparation of the rooms, which shall consist of a reasonable number of employees in order to be able to offer adequate, quality service.

4. The guests will be provided with cleaning and ironing services, whether within the establishment or through a laundry service. The cost of these services may be charged to the guest.

5. The guests shall be permitted to enter or leave their rooms at any time of the day or night.

§9(d)-6. Recruitment and Training of the Employees of an Exempt Business. Exempt Businesses shall provide their clients with attentive, friendly and courteous service. With this in mind, they shall comply with the following requirements:

A. They shall recruit competent personnel for each working area. Alternatively, the recruited personnel shall be adequately trained.

B. They shall conduct trainings for the staff in the areas which they deem necessary.

C. They shall submit to the Hotel School of the Tourism Company a list of its employees indicating the immediate needs for each occupational group, and they shall coordinate with the School the trainings required for the professional improvement of each group. The Tourism Company may require that said trainings include the courses they deem necessary.

D. They shall offer or coordinate, for each employee at the management or supervisory level, courses on motivation, supervision, human relations and professional development.

E. They shall submit to the Tourism Company, for their consideration and approval, an annual training plan for their personnel.

§9(d)-7. Requirements for Operating Exempt Businesses.

A. Exempt Businesses shall faithfully comply with the laws and regulations of the Commonwealth of Puerto Rico and of the United States of America which are applicable to them. The Tourism Company may issue an order to cease and desist directed towards any Exempt Business which violates any provision of said laws or regulations and/or may impose upon it an administrative fine which, except for specific provi-

sions to the contrary, shall not be less than \$100.00 nor more than \$1,000.00.

B. Exempt Businesses shall require of their managers, administrators and the personnel who work in the areas of the kitchen, beverages or uniformed services, a valid certificate of health issued by the Department of Health of the Commonwealth of Puerto Rico. Proof of compliance with this provision must be available during any inspection carried out by the Tourism Company.

C. Exempt Businesses with dining or restaurant facilities shall have competent kitchen personnel to prepare the meals in an adequate and attractive manner. The quality and quantity of the portions shall be adequate for the prices charged. These shall correspond with the description which appears in the menu.

D. Anyone who operates, administers or is the owner of an Exempt Business shall send to the Tourism Company on a monthly basis a daily list of the total number of guests or users of its facilities and where they come from. Likewise, they shall send on an annual basis proof that they have fully complied with the requirements mentioned in subparagraphs 18, 19, 20, 21, 22 of §9(c)-1 hereof, specifying the percentage of net income invested in each of the subparagraphs mentioned above.

E. The Exempt Businesses shall notify the Tourism Company in advance of their intention to sell, lease and/or

change commercial operations, as well as the names of the interested parties and any change in administration. When an Exempt Business assigns or leases any of its facilities, the lessee as well as the lessor (grantee) shall comply with the provisions of this Regulation. The Exempt Business shall also be responsible for the lessee complying with said provisions.

F. The Exempt Businesses shall maintain and submit to the Company, upon the latter's request, their latest audited financial statements, as well as any additional information related to their operating income and expenses. Likewise, they shall allow the officers of the Tourism Company to examine their financial books and files.

G. The Exempt Business shall present an invoice to their clients prior to charging them. Said invoices shall contain an itemization of the various services rendered and their respective amounts.

H. The Exempt Businesses shall maintain a book or any other alternate system for receiving comments and recommendations by the guests and users of their facilities. Such comments shall be taken into consideration in order to correct deficiencies, and may also serve as the basis for advertising campaigns. The Exempt Businesses shall notify the Tourism Company of the complaints mentioned. The Exempt Businesses shall maintain the aforementioned book or alternate system in an accessible place so that the Tourism Company officials may examine it during their periodic inspections.

I. The Exempt Businesses shall submit for the consideration and approval of the Tourism Company and other Government agencies involved, the blueprints and specifications of any improvements or expansion projects of the Business' facilities and/or the installation of signs.

J. No hostelry shall exclude the general public from their surroundings, gardens, beaches, flower shops, beauty salons, restaurants, bars, stores and similar establishments. They may, however, exclude the general public from the swimming pools, tennis courts, golf courses, gymnasiums, and other sports or recreation facilities. This provision shall not apply to Guest Houses.

K. Hostelries shall regularly submit to the Tourism Company the rates for each room.

§9(d)-8. Authority of the Director to Impose Additional Requirements; Cancellation of a Concession; Notice; Procedure.

The Director shall retain the authority to require that the Exempt Business fully comply with the norms set forth herein or with any other applicable regulation or law throughout the period of effectiveness of the Concession. Failure to comply with such norms or with the conditions under which the Concession was issued shall empower the Director to initiate a procedure directed to the cancellation of the Concession, after compliance with the provisions of the Uniform Administrative Procedure Regulation of the Tourism Company.

Any decision following the aforementioned procedure shall be notified to the Exempt Business by certified mail and shall include the grounds upon which the decision was based, as well as the availability of a procedure for reconsideration and the terms thereof, pursuant to the provisions of the following paragraph.

The Exempt Business affected may request, through a written document directed to the Director, reconsideration of its case within the term of thirty (30) days, following receipt of said notice. Said document shall include the relevant facts and arguments. In this regard, an administrative hearing shall be granted, pursuant to the provisions of the aforementioned Uniform Administrative Procedure Regulation of the Tourism Company.

§11(a)-1. Tourism Investment Capital Fund; License; Requirements; Procedure. All applicants for a license to operate as a Tourism Investment Capital Fund shall submit to the Director an original and a copy of a form or Application for License which shall contain the following information:

1. The applicant's name or business name
2. The address of the principal office and agent in charge
3. Employer social security number

4. Name or business name of the Fund (a Fund may not adopt a name or business name identical to that of another pre-existing Fund)
5. Address of the principal office of the Fund and of its authorized representative
6. Name, address and employer social security number of the Developer(s) of the Tourism Project in which the Fund shall make its Eligible Investment.

All license applications shall be signed and sworn before a Notary Public. The information required in the forms prescribed by the Regulation to be issued by the Commissioner pursuant to the provisions of the Act, as well as the instructions included therein, shall be considered to be part of this Regulation.

All license applications shall be accompanied by a certified check or money order payable to the Director in the amount of \$2,000 for the license fees. This amount shall not be reimbursed in the event the license application is denied.

§11(a)-2. Criteria to be Used in Determining the Granting of a License.

A. After the filing of an application for a license, including any information required by the Director and by this Regulation, and after the corresponding fees are fully paid, the Director or his authorized agents shall conduct whatever investigations they deem necessary to determine whether the

license requested shall be granted, taking into consideration the following criteria:

1. The nature and general reputation, economic solvency, commercial and financial experience of the petitioners, promoters, directors or managing partners of the petitioners.
2. The nature and general reputation, knowledge, commercial and financial experience of the officers, directors and/or managing partners who will be directing the Fund's operations.
3. That the Fund will function in accordance with the purposes and requirements set forth in the Act and this Regulation.
4. That the Fund is being created to invest in a (i) Tourism Project which was not under construction at the time the Act was approved, that is, new Tourism Projects, or (ii) program of substantial renovation or expansion of an Existing Business, or (iii) to facilitate interim financing for the construction of and to assume an equity position in the Exempt Business.
5. That the Fund is not being created to invest in an Existing Business unless it is for purposes of raising the equity necessary to carry out the substantial renovation or expan-

sion program required by the Act and by this Regulation.

6. That the Exempt Business is adequately funded, that is, that there is an investment on the part of the Developer(s) or Investor(s) equal to at least 20% of the total cost of the Tourism Project.
7. When the Fund raises its capital through a public or private offering, it shall comply with the provisions of the Uniform Securities Act of Puerto Rico and its regulation. The Director shall impose as a condition that the Fund not raise more than 20% of the total cost of the Tourism Project and that the Exempt Business in which the Eligible Investment is going to be made has obtained from the financial institution which will provide the funding for the Project, or from the Puerto Rico Authority for the Funding of Industrial, Tourism, Medical, Educational and Environmental Control Facilities ("AFICA") a commitment letter stating that it has approved the loan or the necessary bond issue, as the case may be, to complete the Tourism Project.

B. The Director may issue the license once the applicant or applicants have complied with the foregoing

requirements. The license shall include the name and address of the Fund, the date of issuance and the expiration date. Upon the issuance of the license, the Director shall forward to the Office of the Commissioner the copy of the application file which is in the records of the Tourism Company so that the Commissioner may fully comply with the investigative responsibilities imposed upon him by the Act and by this Regulation.

C. The Director may deny a license to operate as a Fund for any of the following reasons (the enumeration is illustrative and not exhaustive):

1. The financial and economic condition of the applicant or applicants, or that their commercial and financial experience is not sufficient to guarantee that the Fund will function efficiently.
2. The applicant or applicants refuse to give the information requested, or submit false information, or refuse to comply with any order issued by the Director by virtue of the authority conferred upon him by the Act and by this Regulation.
3. The officers, directors and/or managing partners who will administrate the Fund do not have sufficient commercial and financial experience to assume such administration.

4. The applicants, officers, directors and/or managing partners who are going to administer the Fund do not have the moral reputation suitable for establishing or directing the Fund.
5. All of the Tourism Investment Capital Funds available under Article 15(c) of the Act for the year in which the application was filed were authorized, prior to the filing of the application.
6. The proposed Fund does not meet the requirements or purposes of the Act and of this Regulation or it is contrary to the public policy of the Commonwealth of Puerto Rico.

D. Any person, officer, director or managing partner who administers a Fund, shall act in his capacity as fiduciary on behalf of the Fund and of the Participants thereof. Thus, his actions must be performed diligently and honestly, and he shall not violate or allow the violation of any of the provisions of the laws or regulations in effect.

E. All authorized Funds shall maintain in effect a bond in order to cover any loss resulting from misappropriation or embezzlement of funds, fraud, abuse of trust and other similar and insurable losses due to the actions of the directors and officers of the Fund or of the firm administering the same, as well as of any employee or agent of the

Fund or of the firm administering the same with access to money, securities and other similar assets. Such bond shall be obtained from a surety authorized to do business in Puerto Rico by the Commissioner of Insurance, and with sufficient resources to respond for any claim made. The bond for each person covered shall be for an amount proportional to the assets of the Fund, according to the following table:

<u>ASSETS OF THE FUND</u>	<u>MINIMUM BOND</u>
Up to \$1,000,000	\$ 50,000
\$ 1,000,001 to \$ 5,000,000	\$100,000
\$ 5,000,001 to \$10,000,000	\$150,000
\$10,000,001 to \$20,000,000	\$200,000
\$20,000,001 to \$30,000,000	\$300,000
\$30,000,001 to \$50,000,000	\$400,000
Over \$50,000,000	\$500,000

§11(b)-1. Certificate of Eligibility. Once the Fund is duly licensed by the Director, the Director shall issue the endorsement and certificate of eligibility for the Exempt Business in which the Fund will make its Eligible Investment. Such license, endorsement and certificate of eligibility shall not be issued in any case in which the capital investment of the Developers or Investors in the Exempt Business is less than 20% of the total cost of the Tourism Project.

§14-1. Fund's Capital; Payment of Issuance Fees. The Fund's capital shall consist of the cash received from persons who

purchase participations in the Fund. The Fund may not make loans or take money on loan.

§14-2. Offerings; Compliance with the Puerto Rico Securities Act. If the Fund is going to issue its Securities in a public offering, it must comply with the applicable securities regulations and previously pay the fees set forth in the Uniform Securities Act of Puerto Rico, Act Number 60 of June 18, 1963.

When the Fund offers its Securities in a private offering, as this term is defined in the Uniform Securities Act of Puerto Rico, it must request the approval of the Commissioner through a letter accompanied by all of the documents related with the offering and the payment of the filing fee, as required by Article 305(e) of the Uniform Securities Act.

§14-3. Suitability of the Participants; Files. The Commissioner, through the regulation which shall be promulgated pursuant to the provisions of the Act, shall establish the criteria to be used to determine the moral, intellectual and financial capacity of each potential Participant in order to determine whether his economic condition is adequate or not to assume the risk involved in the investment.

In addition to the file of each Participant, each Fund shall maintain a Register of Participants which shall contain the following information:

1. Name and address
2. Social security number

3. Investment dates
4. Employer social security number, if applicable
5. Number of securities acquired in the Fund
6. Amounts paid
7. List of the Fund's Participations in other
Tourism Investment Capital Funds
8. Dates of transfer or sales of the Fund's
Securities

The file of each Participant shall be kept for four (4) years after having transferred or liquidated his investment.

§15(a)-1. Renewal of a Fund's License. A Fund may request the renewal of its license if it complies with the following requirements:

1. Submit the original and a copy of an application for license renewal to the Director within a period no greater than six (6) months and no less than ninety (90) days from the date of expiration of the license.

2. In addition to the application for license renewal, the applicant shall submit the original and a copy of the following information to determine whether the license must be renewed:

- a. Evidence which shows compliance with the purposes set forth in the Act during the period in which it has been operating.

b. Experiences in the operation of the Fund during the original period, in terms of the administrative capacity and yield of the Fund.

c. Need to continue operations after the expiration date, in order to provide greater benefits for the Participants.

d. That the liquidation of the Fund will result in an economic loss for the Participants.

§15(b)-1. Fees for Issuance of Participations in a Fund; Disposition of Fees Paid. Each Fund shall pay to the Commissioner $\frac{1}{2}\%$ of the amount of the product of the sale of securities authorized to be issued by the Fund.

§15(b)-2. Escrow Account; Disposition of the Funds Contained Therein. Once the offer has been completed as authorized by the Director pursuant to §11(a)-2 hereof, the depository bank shall issue to the Commissioner a check payable to him in the amount of $\frac{1}{2}\%$ of the securities issued pursuant to Article 15(b) of the Act. The remaining funds in the escrow account shall be available to be used by the Fund as set forth in the escrow agreement and pursuant to the purposes of the Act. Should the capital required not be raised, or should the Tourism Project not be able to close its financing according to the method provided in §5(a)-10 hereof within the term set forth in §22(a)-1, the depository bank shall notify the Participants that their funds are available for reimbursement or reinvestment in another authorized Fund, at their option.

From time to time, the Commissioner shall request of the Department of the Treasury that it transfer to the Puerto Rico Tourism Company half of the funds collected from the Funds pursuant to Article 15(b) of the Act.

§15(c)-1. Maximum Amount of Participations in a Fund that may be Issued; Limitations. The Commissioner shall authorize the issuance of participations in the Funds as long as the aggregate value thereof does not exceed \$200 million per calendar year.

§15(c)-2. Carryover of the Difference Between the Participations Issued and the Limit Established. Notwithstanding the foregoing, if in a particular calendar year, commencing with the year of effectiveness of the Act, the Commissioner does not authorize the issuance of participations in Funds for a total amount of \$200 million, the balance not authorized may be used by the Commissioner in subsequent calendar years to authorize the issuance of participations in Funds in excess of \$200 million.

§15(c)-3. Sale of the Highest Possible Number of Participations. The Director shall promote the sale of the highest possible number of participations in the Funds which are authorized pursuant to the following criteria:

1. In the event that applications are filed to establish Tourism Investment Capital Funds in excess of the \$200 million and the results of the investiga-

tions are satisfactory, the Director shall authorize:

- i. those Funds which allow the greater number of Participants and the best geographic distribution thereof;
- ii. those Funds which in the Director's opinion best promote the purposes of the Act;
- iii. those Funds which have the greatest possibilities of success taking into consideration the financial and commercial capacity and experience of the administrators of each Fund.

\$15(c)-4. Minimum Amount per Participation. The minimum amount to be invested in any Fund shall be \$1,000 per Participant. The manager of each Fund shall be responsible for making participations available to the greatest number of Participants in the Fund under his administration. The Commissioner shall ensure strict adherence to this norm.

\$15(c)-5. Developer Cannot be a Participant; Maximum Amount to be Invested by a Fund. No Fund may invest in an Exempt Business in which the Developer of the Tourism Project is a Participant in the Fund. In the event that the Developer of the Tourism Project is not a Participant in the Fund, the Fund may invest up to 20% of the total cost of the Tourism Project.

\$15(c)-6. Discretion of the Director. The Director may, if the particular circumstances justify it, vary any amount,

percentage or participation mentioned in this section which is not expressly fixed in the Act.

\$15(d)-1. Reports; Responsibility. It shall be the primary responsibility of the manager of each Fund to ensure the correctness of the reports filed and that the Fund makes the investment for which it was authorized pursuant to the Act.

\$15(d)-2. Audits. The Commissioner, through his officials and employees, shall conduct annual audits or inspections in order to examine the books, papers or documents related to the operation of the Fund which are required by this Regulation and by the regulation to be promulgated by the Commissioner pursuant to the provisions of the Act.

\$15(d)-3. Costs. The Commissioner shall collect the amount of \$2.00 for every \$10,000 in Fund assets for each annual audit which is performed on said Fund.

\$16-1. Reports. Each Fund shall submit to the Commissioner those reports which are required by the regulation to be promulgated by the Commissioner pursuant to the provisions of Article 26 of the Act.

\$17(a)-1. Penalties; Dissolution. The Commissioner may impose and collect an administrative fine pursuant to the provisions of the Regulation which shall be issued pursuant to the provisions of the Act, when he finds that for any particular tax year the Fund failed to comply with any of the

requirements, obligations or duties set forth in the Act or any of its regulations.

In these cases, the Commissioner shall enter an order duly notifying the Fund that the order has been issued and the reasons for imposing the fine. If the Fund to which the administrative fine was imposed is not in agreement therewith, it shall request a hearing in writing within ten (10) days following the date of notice thereof. If the Fund is in agreement, it shall pay the fine no later than ten (10) days after the date of notification at the Office of the Commissioner of Financial Institutions through check or money order payable to the Director. If a hearing is requested and held, the Commissioner may confirm or vacate the fine imposed. The Fund may use the remedy provided in §17(a)-3 hereof against the ruling of the Commissioner confirming the fine.

§17(a)-2. Revocation of Licenses. When an event of non-compliance includes three (3) or more violations of the provisions of the Act, or of the regulations promulgated thereunder, or when three (3) or more events of non-compliance occur, the Commissioner may hold an administrative hearing to determine whether the Fund's license should be revoked.

§17(a)-3. Procedure. Within thirty (30) days following the date of notice of the Commissioner's ruling confirming the fine imposed or revoking the license, the Fund may request of the Superior Court, San Juan Part, that it review the decision

of the Commissioner through a writ of certiorari, to be issued at the discretion of the court.

§19(a)-1. Taxation of the Fund and the Participants; Basis Adjustment. All distributions made by a Fund to its Participants shall be exempt from income taxes and shall reduce the adjusted basis of the Participant's participation in the Fund, as long as said adjusted basis is not less than or equal to zero.

§19(b)-1. Distributions to the Participants. All distributions made by a Fund to its Participants which are in excess of the Participant's adjusted basis shall be 90% tax exempt. The remaining 10% shall be subject to taxation pursuant to the applicable provisions of the Income Tax Act.

§19(b)-2. Examples. (i) In the year 20X0, Participant A invests \$100,000 in participations in a Fund. His adjusted basis in said investment is \$100,000 before making any adjustments for tourism investment tax credits or for distributions from the Fund. In 20X1, the Participant takes a tourism investment tax credit of \$25,000 and in 20X2 he takes another tourism investment tax credit of \$25,000. He also receives distributions from the Fund as follows: 20X2 - \$15,000; 20X3 - \$25,000; 20X4 - \$25,000. The adjusted basis and the Participant's tax liability in each year shall be as follows:

20X0 adjusted base	\$ 100,000
20X1 base adjustments:	
(a) tourism investment tax credit	(25,000)
20X1 adjusted base	<u>\$ 75,000</u>
20X2 base adjustments:	
(a) tourism investment tax credit	(25,000)
(b) distribution of the Fund	(15,000)
20X2 adjusted base	<u>\$ 35,000</u>
20X3 base adjustments:	
(a) distribution of the Fund	(25,000)
20X3 adjusted base	<u>\$ 10,000</u>
20X4 base adjustments:	
(a) distribution of the Fund	(25,000)
20X4 adjusted base	<u>\$ 0</u>
Taxes owed for distribution of the Fund	
in excess of the adjusted base	
(\$15,000 x 90% exemption x 36% tax rate) <u>\$ 540</u>	

§21(a)-1. Revocation of License and Liquidation of a Fund; Consequences for the Participants. The Commissioner, with the written consent of the Director, shall revoke the license of a Fund for violations of the Act or its regulations. In the execution of a ruling of this nature, the Director shall comply with the provisions of the Uniform Administrative Procedure Act, Act No. 170 of August 12, 1988, as amended. In these cases, or when pursuant to §15(a)-1 of this Regulation the renewal of the license of a Tourism Investment Capital Fund is denied, the Director shall create a Trust or shall authorize the creation of another Fund which will receive the assets of the Fund revoked and shall continue the operations thereof.

§21(b)-1. Revocation of License; Creation of Trust or New Fund; Adjusted Base. The Participants in the Fund which ceases operations due to non-renewal or revocation of its license, shall receive in exchange for their participations in said Fund, participation in the Trust created by the Director or in the new Tourism Investment Capital Fund authorized by the Director.

The adjusted basis of the Participant in the participations which he receives in the new Trust or Fund in exchange for those he had in the Fund whose license was revoked, shall be the same as the adjusted basis of the participations which he had in the dissolved Fund. Likewise, the Participants in the new Fund shall enjoy all of the rights and benefits granted by the Act, just as if they had continued to be Participants in the dissolved Fund.

If the Commissioner considers that the public interest and the protection of the Participants requires it, he may appoint a trustee to administer or liquidate the Fund instead of following the aforementioned proceedings.

§21(b)-2. Liquidation of a Fund. Any Fund whose license has been revoked for violation of the Act or its regulations, and which has not been replaced by the Director through the creation of another Fund or Trust, shall be liquidated, unless the Director has appointed a trustee to administer such Fund.

§21(b)-3. Grounds for the Liquidation of a Fund. A Fund may be liquidated for the following reasons:

1. For violations of the provisions of the Act or its regulations.
2. For changes in the officers, directors and/or managing partners of the Fund which result in an administration which is deficient or in violation of the provisions of the Act or its regulations.
3. If the Fund fails to operate pursuant to the purposes set forth in the Act or its regulations.
4. If the Fund's administrative expenses exceed the total percentage of the Fund's assets as determined by the Commissioner pursuant to §26(b)-1 hereof.
5. At any time in which the assets of the Fund decrease by 20% or more due to mismanagement.
6. When the Fund fails to comply with any order of the Director or the Commissioner issued pursuant to the provisions of the Act or Act Number 4 of October 11, 1985.

§21(b)-4. Liquidating Agent. In order to carry out the liquidation, the Commissioner shall appoint a liquidating agent who within thirty (30) days of his appointment, shall conduct an inventory of all of the assets and liabilities, and shall prepare a report which he shall send to the Director, the Commissioner, the Secretary and to each of the Participants. If necessary, said term may be extended by the Commissioner.

§21(b)-5. Bond. The liquidating agent shall post a bond prior to taking possession of his duties. The Commissioner shall fix the compensation which he shall receive for his services.

§21(b)-6. Capital Dividends. As soon as possible after the Fund's debts and the fees of the liquidating agent have been paid, the Participants shall receive a capital dividend from the Fund, in proportion to their participation.

§21(b)-7. Records of a Fund in Liquidation. The books and papers of the Fund in liquidation shall remain under the responsibility of the liquidating agent until the full liquidation and payment of all of the legitimate claims against the Fund. Subsequently, they shall be filed with the Office of the Commissioner, provided that such books and papers may be destroyed by the Commissioner five (5) years after the liquidation and final distribution of the Fund's capital.

§22(a)-1. Escrow Account; Temporary Investments. The money which the Fund receives from the sale of participations shall be deposited immediately, in its entirety, in a special escrow account in a commercial bank of recognized solvency under the conditions set forth by the Commissioner, until the Fund closes the offering and the Exempt Business closes the necessary financing for the total construction of the Tourism

Project, or until the 15th of April following the date of creation of the Fund.

§22(b)-1. Temporary Investments. The funds in the escrow account may be temporarily invested as provided by the Director. The gains generated by these temporary investments shall enjoy all of the exemptions granted by the Act and shall not be subject to the provisions of Article 18(c) of the Act.

§22(c)-1. Administrative Expenses. All of the administrative expenses of the escrow account shall be paid for by the Developer of the Tourism Project in which the Fund shall make its Eligible Investment.

§24-1. Sales or Transfers of Securities from a Fund. Unless prohibited by the Fund's Charter or By-laws, any Participant may sell, assign or pledge his participation in a Fund, provided that the tourism investment tax credit may only be taken, as provided by Article 5 of the Act, by those Participants who were registered as such in the Fund at the time of the closing of the financing for the Tourism Project as provided by §5(a)-3 of this Regulation, or who purchase participations in a Fund for which the tourism investment tax credit available has not been fully taken. The purchaser of a participation in a Fund in the secondary market shall request of the seller a certificate of the Fund which shows the amount of tourism investment tax credit taken by the Seller.

§24-2. Administration of the Fund; Registration of Participants. Neither the Developer of the Tourism Project nor any entity related therewith may administer the Fund created to make an investment in the Developer's Tourism Project. Any person who administers a Fund shall duly register any change in the Participants in the Fund, and shall include the information required in §14-3 hereof. No person shall be considered a Participant in a Fund for purposes of Article 5 of the Act unless he appears duly registered in the Fund's Registry of Participants.

§26(a)-1. Public Offerings. A Fund may raise its capital through public or private offerings of participations in the Fund.

§26(a)-2. Public Offerings; Commissions. In the case of public offerings made through underwriters, it shall be illegal to collect or deduct a sales commission greater than the commission approved by the Commissioner through an application therefor. When the sale is made through promoters, officers, directors and/or managing partners of the Fund, no commissions shall be paid. Likewise, no commissions shall be paid for sales made to promoters, officers, directors of managing partners of the Fund.

§26(a)-3. Private Offerings; Commissions. When participations in a Fund are offered through a private offering, no commissions shall be paid for the sale of said participations

to promoters, officers or directors thereof, pursuant to Article 402(b) of the Uniform Securities Act of Puerto Rico.

When the private offering is made through an underwriter, the Commissioner shall determine the percentage of commission to be permitted for each transaction.

§26(b)-1. Administrative Expenses of the Fund. The administrative expenses to be paid by the Fund shall be authorized by the Commissioner and will be based on a decreasing percentage of the total assets of the Fund. Thus, the higher the assets, the lesser the percentage of authorized expenses. The total percentage of the assets of a Fund which may be dedicated to administrative expenses shall be determined by the Commissioner as part of the regulation which he shall promulgate pursuant to the provisions of the Act.

The administrative expenses shall not include the expenses incurred in the evaluation of projects. Said expenses shall be paid by the projects themselves.

§26(b)-2. Public Offerings; Expenses of the Offer. The percentage of the product of the sale of participations in a Fund which may be used to cover the expenses of the offer, such as legal and accounting expenses, the printing of prospectus and advertisements, both for public and private offerings, shall be determined by the Commissioner as part of the regulation which he shall promulgate pursuant to the provisions of the Act.

§26(c)-1. Prospectus; Contents; Requirements. Any prospectus, pamphlet, bulletin, leaflets, advertisements or any sales literature or advertising material directed, or intended to be distributed, to potential Participants, must take into consideration the norms set forth in the Uniform Securities Act of Puerto Rico, and specifically Rules S-1 (Prospectus), S-7 (Advertisement for Securities), S-8 (Delivery of Prospectus) and S-9 (Filing of Sales Literature) of the regulation of the Uniform Securities Act of Puerto Rico and the Federal Securities Acts administrated by the Securities and Exchange Commission and the National Association of Brokers, as well as the criteria regarding these matters contained in the regulation to be promulgated by the Commissioner pursuant to the provisions of the Act.

§26(d)-1. Minimum Investment by the Developers. The Developers of the Tourism Project shall be required to make an equity investment of at least 20% of the total cost of the Tourism Project.

§27A-1. Limited Liability of the Grantees. Notwithstanding the provisions of the Civil Code regarding the obligations of members of a partnership toward third parties, those partners who are members of a partnership organized under the laws of Puerto Rico or of any other jurisdiction which is the grantee of a Concession for tax exemption under the Puerto Rico Tourism Development Act of 1993, Act No. 78 of September 10,

1993, or any successor act of a similar nature, shall enjoy limited liability regarding the debts and obligations thereof, in the event that the partnership capital is not sufficient to cover the same. Provided, that said limited liability shall benefit the partners with respect to all of the activities of the partnership, including, but not limited to: (i) claims arising from the tourism activities object of said Concession; (ii) activities related to the liquidation and termination of said activity; (iii) activities related with the disposition and transfer of the properties used therein; and (iv) activities related with the operation of any casino which is operated under a franchise granted pursuant to Act No. 221 of May 15, 1948, as amended, or any successor act of a similar nature. Provided, further, that the benefit of limited liability provided herein shall commence on the date of the filing of an application for exemption under Act No. 78 of September 10, 1993, and shall apply to any cause of action which arises from facts which occur prior to the liquidation of the partnership.

§27A-2. Examples. (i) The partnership activities of X, a special partnership under Supplement P of the Income Tax Act of 1954, are the operation of Hotel XXX, its casino, located on the Hotel's premises, and four discotheques located outside the Hotel's premises. In 1997, two years after obtaining its Tax Exemption Concession under the Act for the operation of the Hotel, Special Partnership X ceased to qualify as a

special partnership for failure to comply with the minimum requirements of Supplement P. In 1999, the partners of the now Civil Partnership X decide to cease doing business as a partnership. They begin to liquidate the partnership and distribute all of its assets among its partners. The partners of X comply with all of the legal procedures required to liquidate the partnership in the year 2002. In the year 2004, the partners of X are sued in their personal capacity by a client of one of the discotheques who suffered a fall in 1998 and who had tolled the statute of limitations to file a complaint against the partners of partnership X through extrajudicial claims during the years 1999, 2000, 2001, 2002 and 2003. The partners of X shall not be personally liable for any obligation which arises from said judicial action since said action is based on facts which occurred prior to the liquidation of the partnership.

(ii) Continuing with the same fact pattern, in the year 2000, Partner #1 becomes the owner of the Building on which one of the partnership's discotheques was located as a result of the partnership's liquidation process. In the year 2001, before the partnership is formally liquidated pursuant to the provisions of the Partnership Agreement, a pedestrian becomes injured when he tripped and fell on the premises of said Building. The pedestrian files suit against Partner #1 during the same year 2001. Partner #1 shall be personally liable for the damages suffered by the pedestrian

because, since the title of the Building had passed on to his name, the claim cannot be considered to be a result of partnership activities. The other partners of X shall not be liable for the damages suffered by the pedestrian since they were not partners of Partner #1 with respect to the ownership of the building at the time the accident occurred.


(iii) Under the same fact patterns as example (ii), if ownership of the building passes on to Partner #1 in the year 2002, and the accident occurs in 2001, the partners, including Partner #1, shall not be personally liable for the claim since, although Partnership X had ceased operating and was in the process of liquidation, the partnership had not been formally liquidated pursuant to the provisions of the Partnership Agreement, and the building belonged to the partnership at the time of the accident, for which reason the provisions of Article 27(a) of the Act are in full force and effect.

§28-1. Unconstitutionality. Should any article, section, item, subparagraph, paragraph, clause or part of this Regulation be declared unconstitutional by a court with jurisdiction, the judgment entered in this regard shall not invalidate the rest of this Regulation, and its effects shall be limited to the article, section, item, subparagraph, paragraph, clause or part of this Regulation which was declared unconstitutional.

§29-1. Effectiveness. This Regulation shall enter into effect as soon as the provisions of Act No. 170 of August 12, 1988, as amended, and of Act No. 10 of June 18, 1970, as amended, are complied with.

APPROVED BY THE BOARD OF DIRECTORS AND BY THE EXECUTIVE DIRECTOR OF THE PUERTO RICO TOURISM COMPANY, IN SAN JUAN, PUERTO RICO, ON MARCH 14, 1994.

/s/ Jorge A. Junquera
President
Board of Directors
Puerto Rico Tourism Company



Luis G. Fortuño
Executive Director
Puerto Rico Tourism Company

APPROVED BY THE HONORABLE GOVERNOR OF PUERTO RICO, AT LA FORTALEZA, SAN JUAN, PUERTO RICO, ON MARCH 26, 1994.

/s/ PEDRO ROSSELLO
Governor of Puerto Rico